

INSURANCE BULLETIN

BULLETIN #10

Stretching Your Insurance Dollar

CNA and NESPA are proud to provide you with this information. We trust that you will find it useful in understanding the insurance and risk management issues associated with your business.

Most spa and swimming pool companies today operate on razor thin profit margins, and property and casualty insurance premiums tend to be one of the larger expense items for most spa and swimming pool companies, behind labor and materials/equipment costs. Consequently, spa and swimming pool companies need to spend their insurance dollars wisely. It's simply a matter of knowing what you're buying, understanding what coverages you really need (and don't need) and controlling the variables that influence your premiums.

When you purchase an insurance policy, you're actually buying a package of different coverages, such as property coverage and general liability coverage, or auto liability and auto physical damage coverage. Different parts of the policy protect against different kinds of accidents, occurrences or losses. However, depending on what you're insuring, some of those coverages may not be necessary. Making an effort to identify those areas where you may be overinsured can trim your premiums and still leave your business adequately protected from loss. As always, be sure to seek the advice and counsel of your insurance agent or broker when making changes to your insurance and risk management program.

Rethinking What's Required: Business Automobile Coverages

Many businesses purchase business automobile coverages that may not be needed at all or may not be needed on every vehicle in the company's fleet. Many business owners would be wise to rethink what's really required.

Automobile medical payments — If a non-employee is hurt while riding in one of your company vehicles, "medical payments" coverage in your commercial auto insurance offers what essentially is a "goodwill" payment to the injured party as reimbursement for their medical costs. A couple of decades ago, most people would graciously accept a medical expense reimbursement and be on their way. But in today's litigious society, people are far less likely to accept payment of their medical expenses only for injuries caused by your company, even when there are minor injuries.

So one could reason that if you're going to be sued anyway, what good is auto medical payments coverage? Why not drop this goodwill coverage from my business auto policy and save some premium? Cynical or not, it's a fair question. But, even if you're an optimist, it's wise to consider your own loss experience and whether your potential exposure (injury to third parties and the associated medical costs) justifies the cost of this goodwill coverage.

Uninsured motorist — If you're driving your personal car and are injured in a crash with a motorist who does not have auto liability insurance, uninsured motorist (UM) coverage offers you the financial protection that would have been provided by the at-fault driver's insurance company — if he'd been insured. It's a worthwhile coverage in a personal lines scenario. But, for a business, UM coverage substantially duplicates other coverage you probably already have.

For example, employees driving company-owned vehicles would already be covered by your firm's workers' compensation insurance policy, which offers unlimited medical benefits as well as indemnification for lost wages. For sole proprietors, business owners and others in the company who are not covered by state workers' compensation laws, scheduling UM coverage on their vehicles makes good sense. But since most employees are covered by state workers' compensation laws, you have to wonder if carrying UM coverage on the company automobile policy for all employees is a smart use of your insurance dollar. Be sure to consult with your insurance agent or broker for more information on this subject.

Physical damage (comprehensive and collision coverages) — Physical damage coverage pays for damage to your company vehicles, such as damage caused by hail, theft, or collision with another vehicle or object. On some vehicles, such as trucks and trailers, it might be wise to drop comprehensive coverage while keeping collision coverage. Depending on the age of a particular vehicle or the amount it's been depreciated, insuring it against physical damage may not be critical, especially if the actual cash value of the vehicle is very low. In fact, on older, low-valued vehicles, it's possible that the cost of repair could exceed the depreciated value of the vehicle. In this scenario, you might be better off discontinuing physical damage coverage on such a vehicle and pocketing the premium savings.

Another option to consider is "specified causes of loss" coverage instead of comprehensive coverage. Comprehensive coverage includes the peril of glass breakage. Business owners should ask two questions regarding breakage of glass:

- How often do you break windows or windshields in your company vehicles?
- How much do they cost to replace?

Depending on your vehicles and the answers to the above questions, you might decide this is a cost you could easily self-insure rather than insuring. Many business owners don't realize they can purchase "specified causes of loss" coverage, which is similar to comprehensive coverage but without the glass breakage coverage. It's an option that could lower your auto physical damage premium.

Payroll Recordkeeping

Payroll recordkeeping is an important area that can have a significant impact on premiums. Construction (including spa and swimming pool work) is one of the few industries where workers' salaries can be split among different categories or classification codes for insurance premium/rating purposes. For instance, your firm might do spa and swimming pool construction as well as snow and ice maintenance work in the winter time. If your payroll records are documented properly, it can save you money because these operations are classified separately and are priced using very different rates. Generally, snow and ice work will be subject to much higher rates. If your payroll records are not properly documented, the insurer will rate all of the work based on the snow and ice work classification with the higher rates.

Underwriters develop workers' compensation premiums using the salaries and other compensation you pay your employees. If you pay your employees higher than average salaries because of their special skills or experience, you may be paying higher than average workers' compensation premiums. In this case, you should check to see if a **contractor classification adjustment program** is available in your state. These programs are governed by state law and may provide a payroll credit that lowers your workers' compensation premium.

Overtime pay is another item with a potential impact on the amount you pay for workers' compensation coverage. The rates established for workers' compensation are to be applied only to the base wage paid to employees. If overtime or differential pay is offered to your employees, you will need to accurately track the different scales to be certain you are not over-reporting your employee's base wages. The best way to know if you're paying more than necessary is to review documentation from your insurer's premium audits at the end of the policy period against your payroll and accounting records. If you're entitled to a large refund for the expired policy term because your payroll or sales were less than what was estimated when the policy was written, you might want to consider lowering the sales or payroll estimates on your insurance policy for the current policy term. You should also review your audit to be certain the correct exposures (payroll, sales, number of vehicles, etc.) were used and that the assigned classifications were correct. If you are confused by the classification names or need to determine if alternate classifications would be more appropriate, your agent or insurance company premium auditor should be contacted.

Workers' Compensation "E-mod"

Your workers' compensation claim history drives your company's experience modification rating, also known as your EMR or — more commonly — your "E-mod." Your E-mod not only affects your workers' compensation premiums, but some general contractors and owners may also use E-mods to weed out potentially unsafe contractors during the bid process.

Every insurance carrier reports all of its company's workers' compensation claim data to an independent rating bureau, which then compiles the data. Your company's workers' compensation claims are then compared to what is expected for your type of business, based on the reported payrolls. So, if you're a spa and swimming pool contractor, you are compared with other spa and swimming pool contractors of similar size. The point being that your workers' compensation claims experience is compared with the claims experience of your peer companies and an E-mod is calculated by the rating bureau.

An E-mod calculation gives more weight to the frequency of injuries but does not overly penalize a company for the severity of one particular claim. Every new company starts with an E-mod of 1.00, which then is adjusted in future years, upwards or downwards, based on the company's workers' compensation claims experience. The goal is to have a "credit modifier," which means your E-mod is less than 1.00, which saves you money. If your base workers' compensation premium is \$100,000 and your E-mod is 0.70, your final premium would be \$70,000. Conversely, an E-mod higher than 1.0 is known as a "debit modifier." In the example above, if your E-mod was 1.3, your final workers' compensation premium would be \$130,000 – which means you would pay \$60,000 more for workers' compensation coverage than your competitor with an E-mod of 0.70 and base workers' compensation premium of \$100,000.

Look for Errors

Obviously, you can affect your E-mod by working to prevent claims through safety and loss prevention. But it's also possible to improve your EMR by simply checking for errors in the data that is submitted to the rating bureau and making corrections where warranted.

Each year, your insurer sends your loss information to the rating bureau on something called a "unit stat card." You should take ownership of the information on that card because the E-mod that results from it is so important to your business. If your agent can't provide the actual card, he or she will give you the information that makes up the unit stat card. Before the card is submitted to the rating bureau, you should examine it with an eye toward these potential red flags:

- **Reserves** — When you report a claim, it is recorded on your card even if there is no injury and nothing ultimately is paid. Sometimes, when the claim is recorded, an insurer will enter a reserve amount in anticipation of a future settlement or payment. You need to ensure that claims with no payments are accurately recorded as such.
- **Incorrect payroll coding** — If a spa and swimming pool worker's payroll is coded as a clerical payroll by mistake, for example, there's a good chance that your firm's losses will appear to be much higher than average. That's because it's assumed that a clerical person will generate fewer workers' compensation claims than a spa and swimming pool worker. You could be assigned a debit modifier simply because your expected losses were underestimated due to a coding error.
- **Premiums paid** — Your unit stat card will show the premium your company is paying. If the premium amount recorded is less than what you actually are paying, then your expected losses probably are lower than your actual losses, and you'll have a debit modifier. So, make sure every nickel you've paid is reported.
- **Subrogation** — When insurers sue third parties to recover amounts paid to or on behalf of their policyholders, that's called subrogation. For instance, suppose one of your employees was injured by a defective piece of equipment and your workers' compensation insurer paid \$50,000 for the injury. If the insurer sued the equipment manufacturer and was able to recover \$40,000, your card should reflect only the \$10,000 difference. If the entire \$50,000 is recorded instead, the oversight will be reflected in your E-mod, which will increase your premium.

Certain Operations and Projects Can Really Cost You

When underwriters evaluate the insurance risk presented by your business, they will often base their opinion on the most hazardous work you do. This isn't unique to business insurance. If your hobby is flying experimental aircrafts, for instance, you would notice that fewer life insurance companies would be willing to offer you coverage. You would also pay higher premiums. On a personal level, the difference in life insurance premiums probably wouldn't cause you to give up flying. But for a spa and swimming pool company, a more hazardous operation or project could have a huge impact on overall insurance premiums.

For instance, some spa and swimming pool contractors have branched out and started constructing indoor pools and spas. Because this work historically results in higher general liability claims for insurers, firms that engage in this work may have fewer companies willing to insure them, and those that do, will likely charge higher rates than for spa and swimming pool companies that do not engage in this type of work. By avoiding high risk, high hazard types of operations or projects, you avoid the higher insurance premiums associated with them.

Review Your Claim History

Many owners and CFO's of spa and swimming pool companies rarely review or even request their claim histories — known as loss runs — unless they're "shopping" their insurance at renewal time. That's unfortunate because loss runs can teach you a great deal about claims that ultimately affect your renewal premiums, including:

- The number of claims you've had (frequency) and the amount of money that's been paid on each claim to-date (severity)
- Trends or patterns that may indicate certain employees, types of jobs or locations generate an unusually high number of claims
- A frequency of low-dollar claims that might be cheaper to self-insure (via a deductible)
- The impact of a single, unusually large claim
- The amount of money "reserved" for open claims that are in the process of being adjusted, but have not yet been closed (this topic is addressed in more detail later in this bulletin)

Implement a Comprehensive Safety Program

With your claim information in hand, you'll be better equipped to understand how to reduce your claims. Your claim data might suggest that your overall safety program should be enhanced in a certain area, such as fleet safety or driver controls, or that new safety equipment would be a worthwhile investment. Your loss runs might illustrate that there are certain jobs that you should subcontract to other companies because your employees don't have the necessary skills to accomplish these jobs successfully, without incurring claims. Or your claim data might suggest that you simply need to add an incentive component to your safety program, such as a safety contest or financial incentive, to focus your employees' attention on problem areas and lead to a change in behavior.

If you have not yet done so, one of the easiest and most effective changes to your safety program is to let your workers know that safety is of utmost importance to the company and has the full support and attention of management and the company owners. So often employees only hear of the need for reducing waste, working faster and improving productivity. If you don't take the opportunity to also mention the importance of safety, your employees won't know it is important. Safety should be positioned as being just as important as productivity.

Whatever the cause of your claims or the possible solutions you offer, it's critical that your safety and loss prevention program be designed to address the root causes of accidents and injuries. Doing so not only will benefit your company's bottom line, but it also will demonstrate to insurance carriers that you're serious about safety and reducing accidents and injuries.

When it's time to negotiate your renewal policies, insurers will ask you or your agent to explain your losses — why they happened and what you've done to address them and prevent similar events from recurring in the future. If you can demonstrate that you've done your homework and implemented an effective safety and loss prevention program, underwriters will look at your business in a more favorable light, and will be more likely to extend favorable terms, conditions and pricing.

Deductibles — Assume a Little Risk

A final suggestion is to consider assuming "predictable" small losses and use your insurance dollars to protect you from the unpredictable and potentially catastrophic losses. Insurance companies generally prefer their insureds to retain or absorb the first \$1,000 of loss via a deductible because processing claims for such small amounts is time consuming and therefore expensive. For very small claims, it costs the insurer more to process the claim than the claim is worth. Lost tools, crushed cell phones and dented fenders are unfortunate. But you could probably save a few dollars on your general liability, business automobile and equipment insurance by raising your deductibles, ignoring the dents and paying for small tool and equipment losses out of your own pocket.

Through the SPLASH program, CNA can provide a business insurance program that offers comprehensive risk control (safety) services, expert claim handling and property/liability insurance coverages designed specifically for spa and swimming pool professionals. So when your business is insured with the CNA/SPLASH program, you'll have peace of mind knowing it's a program backed by a carrier with more than 60 years experience in the construction industry. Give us an opportunity to earn your business – ask your insurance agent to obtain a quote from CNA and discover how you can benefit from this partnership.

For more information, contact your local independent agent or visit www.cna.com.

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