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Risk Management

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Managing the Contingent Workforce

For most companies, managing human resources will probably require more attention than any other aspect of your risk management plan. Workers' compensation, safety, compliance with wage/hour laws and avoiding discrimination—these responsibilities can keep one or more managers busy full-time. Using contingent workers can relieve your organization of some human resource functions; however, it can create other risk management exposures.

Over the past two decades, contingent work has moved into a wider array of occupations. According to the Bureau of Labor Statistics, by 2008, the types of clerical positions commonly associated with temp work, such as secretary, typist, receptionist, data-entry operator and office clerk, represented less than a quarter of overall temp help services industry employment. Today, you can hire anyone from manufacturing help to a CEO on a contingent basis.

When you hire individuals on an independent contractor basis, they act as their own employer, retaining responsibility for payment of any employment taxes, workers' compensation and insurance, including any professional liability coverage needed. They simply invoice

the employer, often on a per-job rather than a per-hour basis.

When you hire temporary or leased employees, the agency acts as the employer. The agency is responsible for screening employees, paying employment taxes, providing workers' compensation and, in some instances, providing employee benefits. The agency pays the employee directly, invoicing your organization (at a marked-up rate) for hours the employee works.

Professional employer organizations, or PEOs, are similar to temporary agencies, except they handle long-term relationships that involve all or most of a company's employees. The National Association of Professional Employer Organizations (NAPEO) estimates between 2 and 3 million people are currently covered by a PEO arrangement.

Under a PEO arrangement,



the company and PEO enter a contractual agreement to become co-employers and share or allocate employment responsi-

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This Just In

On any one day in 2011, U.S. staffing firms employed an average of 2.8 million workers, reported the American Staffing Association. During the course of the year, more than 12.9 million temporary and contract workers found work through staffing firms.

Temporary and contract staffing is growing, increasing 6.6 percent between May 2011 and May 2012. This trend is likely to continue as the economy continues its tepid recovery, making many employers reluctant to bring on permanent staff. The U.S. Bureau of Labor Statistics projects the employment services industry, which comprises employment placement agencies, temporary help services, and professional employer organizations, is projected to add 631,300 jobs, an annual rate of increase of 2.1 percent, and reach 3.3 million by 2020, placing this industry among those with the largest projected employment growth.

In addition to temporary and contract workers, independent contractors comprise a significant portion of the U.S. workforce. The U.S. Bureau of Labor Statistics estimated there were 10.3 million independent contractors in the U.S. in 2010.

Nontraditional work arrangements can create unexpected risk exposures. For more information, please see the article on this page.



Understanding Surplus Lines

When model Heidi Klum insured her legs for \$2.2 million and guitarist Jeff Beck insured each of his fingers for \$1 million, you can bet a standard insurer didn't cover those risks. These celebrities turned to the surplus lines market. Although your organization probably won't need to insure body parts, you might need the services of the surplus lines market.

Most organizations can meet the majority of their insurance needs in the "standard" insurance market, which consists of "admitted" companies that are licensed to do business in specific states. The state insurance department regulates their coverages and rates. Surplus lines carriers differ in that they are "non-admitted," and they cover risks that admitted companies are unwilling to write.

Although surplus lines insurers are "non-admitted," that does not mean they lack regulation. Each surplus lines insurer must be admitted (licensed) in one of the 50 states and must meet that state's financial solvency requirements. The state of domicile becomes that insurer's regulator.

Surplus lines companies are able to offer special coverages because they are largely free of rate and form restrictions that make it difficult for standard companies to write the risk. Their flexibility allows them to design policies that meet unique customer needs.

Flexibility from the Exotic to the Everyday

In addition to insuring a model's body parts, surplus lines insurers also handle a broad range of more common business risks. NAPSLO, the National Association of Professional Surplus Lines Offices, Ltd., cites these examples of the types of risk commonly insured by excess and surplus lines insurers:

- ✱ A developer re-building homes and businesses in hurricane-prone areas
- ✱ A sports celebrity who wants to insure his or her legs or hands
- ✱ A school district building a new high school
- ✱ A nonprofit that seeks to provide food, medical care and education in Third

World countries

- ✱ A research lab working on a promising, yet unproven new drug
- ✱ A law firm specializing in intellectual property work

Accessing Specialty Markets

Surplus lines companies sell their products through special brokers — called surplus lines brokers or wholesalers — and through managing general agents (MGAs). MGAs (which can be individuals or business entities) hold "appointments" from insurance companies, which give them the authority to solicit insurance applications from agents and negotiate coverage. MGAs generally specialize in particular types of risks and know which insurers are most likely to accept your risk.

The end customer has no direct access to those agents or to the non-admitted market. The good news is you do not need access. When we learn that you have an unusual risk, we discuss it with you and then contact the appropriate wholesaler or MGA to obtain the coverage you need.

Regardless of your special risk exposures, the process of finding the right coverage is largely invisible to you. We place the coverage and you receive a policy, just as you do with your standard property/casualty insurance.

Talk to Us

Sometimes a small change in your business strategy creates a need to access the surplus lines market. For instance, if a contractor installs kitchen cabinets in rental apartment buildings, he probably buys liability coverage in the standard market. However, if he takes a similar job for condominiums, he will probably need surplus lines liability coverage. Why? Because his potential liability is greater. If there were a construction defect, the contrac-



tor could be sued by each condo owner, rather than just one building owner.

If your business activity has changed, give us a quick call, and we'll let you know if we need to make any adjustments in your insurance program. ■

The Nonadmitted and Reinsurance Reform Act of 2010 (NRRRA), part of the Dodd-Frank Wall Street Reform and Consumer Protection Act, affects the placement of nonadmitted insurance throughout the country. The act became effective on July 21, 2011. The NRRRA clarifies that regulation of surplus lines insurance is subject solely to regulations of the insured's home state. This means only the insured's home state may require a surplus lines broker to be licensed to sell, solicit or negotiate surplus lines insurance, and only the home state can collect premium taxes on surplus lines insurance.

Although states regulate insurance activities, "The NRRRA, by its various provisions, will preempt or supersede portions of the excess and surplus lines law as they exist today in the states," reports the National Conference of State Legislatures. Each state must conform its regulations to the NRRRA. ■



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bilities. The PEO generally handles all human resource and benefit management functions. It hires workers, controls payment of wages, provides unemployment insurance and other benefits, and handles employment taxes. The subscribing company retains some employer responsibilities, including supervision, to ensure the delivery of the company's products or services. Smaller employers in particular find advantages in PEOs and leasing.

Benefits of temporary employment or PEO arrangements include:

- ✱ Expert human resource and benefit administration. PEOs and temporary employment agencies can devote full-time, professional staff to these tasks.
- ✱ Better benefits. Larger PEOs and agencies manage thousands of employees, giving them more purchasing power than individual small employers have.
- ✱ Better safety. A PEO should have on-staff safety professionals, who conduct regular audits that could reduce injuries and costs.

Still, using contingent employees can create risk exposures, including:

- 1 Workers' compensation coverage gaps. Some states permit PEOs to provide workers' compensation for their clients. If yours does, ask the PEO for a certificate of insurance as evidence of coverage. And make sure the PEO's policy includes an "alternate employer endorsement" to cover employees injured while working for you.

Even if your PEO provides coverage,

you might want to keep a minimum premium workers' compensation policy in place. A minimum premium policy will provide some protection if your PEO fails to buy coverage or stops making premium payments — just make sure your insurer agrees to cover leased employees as regular employees.

- 2 Lawsuits from injured workers. Even if your PEO or lease arrangement includes workers' compensation coverage, the worker can sue your company for negligence if unsafe or hazardous conditions led to the injury. Most commercial general liability policies exclude coverage for "special employees," such as leased employees or independent contractors. You can remedy this coverage gap by adding the "coverage for injury to leased workers" endorsement.
- 3 Gaps in umbrella liability. Some umbrella policies require you to schedule the underlying employers' liability policy, which is part of your workers' compensation policy. If you have no workers' compensation policy in place, your umbrella might not respond to an employer's liability claim. Having a minimum premium workers' compensation policy could help eliminate this coverage gap as well.
- 4 An organization can still be held responsible for discrimination law violations when using a temporary agency or PEO. To protect your company, consider buying employment practices liability coverage. If you already have a policy, make sure it includes leased and special employees in its definition of covered employees.
- 5 Employment tax liability. When you con-

tract with a PEO, the IRS considers it the "employer of record" for employment tax purposes. However, if you maintain too much control over the employees, the IRS could consider your firm the employer and liable for withholding and Social Security. State laws on leased employees vary. Some states consider the PEO to be the employer, while others consider the PEO a co-employer.

Before entering into a PEO or leased employee arrangement, check the provider's qualifications and references. The Employer Services Assurance Corporation conducts voluntary accreditation for PEOs. See their listing of accredited PEOs at www.esacorp.org. You can also check whether a PEO's risk management staff has earned professional accreditation at www.certificationinstitute.org.

We can review your insurance program to help you manage any employment-related exposures, no matter what type of employees your organization has. For more information, please call us. ■

The Bureau of Labor Statistics defines contingent workers as "persons who do not expect their jobs to last or who reported that their jobs are temporary. They do not have an implicit or explicit contract for ongoing employment." These alternative employment arrangements include persons employed as independent contractors, on-call workers, temporary help agency workers, and workers provided by contract firms. ■

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erage, make sure any valuation you use bases the RR cost value only on property covered under the policy. In most cases this would exclude foundations, underground wiring, finance costs and land values.

Another common mistake is to include renovation or remodeling costs that add little or no value, or to include depreciation costs that have no impact on the RR level. Business

owners also often neglect to regularly update their property valuations to reflect changing market conditions or updated inventories of business-personal property.

"Having an accurate valuation on the property you want to insure is the foundation of successful risk management," says insurance broker Robert Banks. "Small mistakes can compound themselves when it comes to

making a claim. Underinsurance can mean crucial delays in restoring companies to their pre-loss position and can have a huge impact on their financial health. For small companies especially, underinsurance in such cases can be devastating."

For more information on obtaining the right kind and amount of insurance on your company's property, please contact us. ■



Property Valuation: How to Get It Right

Accurately valuing your property is the first step to ensuring effective coverage. If you place an overly high value on your property, you pay more premium than you need to. If you undervalue it, you may not have enough insurance to cover a loss.



Calculating the value of property for insurance purposes can be deceptively difficult. Organizations that use a do-it-yourself approach often make basic errors.

The first question to ask yourself is, what property should be insured? Obviously you will want to insure all buildings and essential structures your organization owns, including all the technology and energy infrastructure they contain. But take care not to overlook other structures such as fences, security systems and parking facilities. The basic property policy does not include coverage

for debris removal and additional costs for constructing to meet current, stricter building codes—consider adding these coverages to avoid unexpected rebuilding costs.

The other major property category is business-personal property. This will include your inventory, office equipment, computers and maintenance equipment.

You can use many different valuation criteria for commercial properties, such as tax assessment valuation, accounting valuation and market worth. Using the purchase price of a property as a starting point is one common error — often it has little relation to re-

placement value.

For insurance purposes, only two valuation methods really matter:

Repair/replacement cost value (RR) — This represents what it would cost an owner to completely replace a facility with all new construction, business-personal property, etc.

Actual cash value (ACV), which is usually defined as replacement cost minus depreciation.

Most commercial property policies use RR. This approach means facilities are rebuilt with new materials after a loss. But some policies still carry ACV provisions. A policy using ACV valuation will generally cost less. Because the insurance company takes depreciation into consideration when paying the loss, it also means that your claim payout will be lower than with an RR policy and might not be enough to restore the business to its pre-loss position.

Calculating the RR value for insurance purposes can present a challenge. You can use yardsticks such as capitalized cost, value per square foot and inflation. However, these indexes may not be relevant for your specific property.

To avoid paying too much for your cov-

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Professional Appraisal Services Can Save Money

Obtaining a professional property valuation can help insureds avoid many common property valuation errors. If your company has significant business personal property, multiple locations, any form of unique construction or sizeable total values, you may wish to consider using a professional appraisal service. When you consider the potential costs of over- or under-insurance, the price of this service could pay for itself in a short time.

A professional appraiser has the advantage of being able to use up-to-date comparative information. Different appraisers have different specialties, so make sure any firm you use has experience evaluating properties like yours.

Appraisers offer a range of services:

- ✦ Developing accurate values by using multiple indexes, modeling approaches and other techniques
- ✦ Calculating depreciation accurately
- ✦ Identifying property excluded in the policy to avoid reporting it
- ✦ Providing documentation that can help prove loss in the event of a claim
- ✦ Providing expert testimony in case of loss.

Some appraisers will offer periodic updating of your property valuations at a reduced charge and appraisals for property difficult to value, such as art. For information on obtaining a property valuation, please contact us. ■