

Risk Transfer

Are You Utilizing It Effectively?

by Jeff Barrett

Insurance can be confusing. One of the most troublesome concepts seems to be the utilization of risk transfer as a tool to limit exposure.

Simply stated, risk transfer is a process by which the responsibility for potential loss is shifted from one party to another, often through the use of insurance or contractual language. One example is the insuring of automobiles. The car's owner "transfers" part of the risk to the insurance company. If a loss occurs, the owner may pay a deductible, but the insurance company pays the majority of the loss. The same principle applies to businesses where the difference lies in the complexity and variety of potential exposure.

Clients generally fall into three categories in terms of strategies for risk transfer:

1. **Group A** has an effective program with constant updates and monitoring.
2. **Group B** makes an attempt to use risk transfer but needs help organizing the program.
3. **Group C** either has no risk transfer program in place or its program is ineffective.

Unfortunately, most companies fall into Groups B or C, which indicates that there is room for improvement in both understanding and implementing a successful risk transfer program. The following are some helpful ways to identify to which group you may belong, as well as the steps needed to make improvements.

Can I do without a transfer strategy?

One answer is, "Sure, if you're absolutely certain that you'll never find yourself in a situation where you have to accept liability without having proper coverage." That sounds like a situation you'd prefer to avoid, but it can happen if you don't really understand the type of coverage you have in place. No wonder some people call this "being an unknown self-insurer." Another answer is, "No, if your goal is to be responsible only

for your own negligence—and not someone else's." A planned strategy can ensure that you are covered for your own actions (or failure to act) and help you avoid becoming liable for acts or failures to act of other parties.

A transfer strategy formally identifies your risk limits, as well. You don't have to guess what's covered or for how much.

And the final answer is, "No, because a risk transfer strategy can keep you from becoming an inadvertent participant in the current trend of passing liability to others." This is a practice some vendors and customers use to avoid having to assume liability themselves. With a formal program, if an outside source puts pressure on you, you can refuse to accept liability for a situation for which you are not really liable.

So which group am I in?

The simplest way to identify the type of risk transfer program you have (or don't have) is to answer a few "yes" or "no" questions. Keep track of the "yes" answers and you'll be able to determine your group once you're finished.

- Do you review every contract you are asked to sign?
- Have you ever returned to the customer/vendor who provided a contract and negotiated changes more favorable to you?
- Does your legal staff or insurance broker help identify potential risk issues?
- Have you ever rejected a contract because the terms and conditions were unacceptable to you?
- Does your business have an organized procedure for maintaining certificates of insurance and keeping them readily available if needed?
- Do you review your certificate list each year and remove companies with whom you no longer do business?
- If your employees use personal vehicles for company business, do you routinely review the liability limits on those vehicles?



- Can you identify the difference between the insurance section and the indemnification provision on your insurance contracts?

Although it's certainly not scientific, the number of "yes" answers can give a general idea of your risk strategy group. The total of "yes" answers may identify you with one of the following groups:

- 6-8 You more than likely have an effective risk transfer program (Group A)
- 3-5 You have a program in place, but it could be more effective (Group B)
- 0-2 You either have no program or there's a good chance that your program is not serving your needs. You may want to seek advice to effectively transfer risk. (Group C)

What does this really mean?

Now that you know more about risk transfer and you've established your probable risk transfer status, let's review a few common problems that have the potential to create major roadblocks for a successful risk transfer program.

A certificate that doesn't meet the terms and conditions of the contract is sent out without changing the contract. This situation has the potential for disaster. Some clients believe that a vendor or customer bears responsibility for failing to recognize the difference between the proposed contract and the final contract. The truth is that the insured is responsible. Failure to notify may result in the insured unknowingly becoming self-insured.

Failure to understand the difference between Primary and Non-Contributory language. Primary language is generally not as problematic as non-contributory language, which may unintentionally eliminate your carrier's ability to seek subrogation for negligent acts on the part of your customers or vendors.

Notification in the event of cancellation or material change in coverage or limits. Certificate language often

states that the carrier will "endeavor to notify" you in the case of cancellation or change in coverage or limits, but notification is not guaranteed. However, some carriers may be willing to modify this language. Be sure that you check with the insurer to verify the wording of this statement.

Difference between "named insured" and "additional insured."

Use of the language "any" or "all" regarding acts of negligence.

Waiver of subrogation. This action generally requires the carrier's acceptance. Some carriers will grant a "blanket waiver of subrogation," which almost always needs to be requested in the contract language. Be sure that each coverage line is identified, as some carriers may not accept waiver of subrogation for all coverage lines.

In the event you indemnify clients or vendors, you must choose counsel that is acceptable to the indemnified party. This will not be acceptable to your carrier. Most policies include "duty to defend" language, and only your carrier has the right of defense and settlement.

Temporary Staffing Companies. You may need to make several changes to your workers' compensation and general liability policies to ensure that you are protected.

This is by no means a complete list of potential problem areas regarding risk transfer. As contracts become ever more complex, you may need help navigating through the contractual language. Your broker can be a good resource for insurance-related questions and legal counsel can answer questions about indemnification contractual provisions. Risk transfer is a growing area in the insurance industry. Business owners who fail to learn as much as possible about this topic could put themselves, their organizations and their employees in jeopardy.