The Vermont Legislative Research Shop

Using Captive Insurance Model for Socially Responsible Corporations

This report examines the captive insurance industry in Vermont and how it might be used as a model for socially responsible corporations.

Captive Insurance

A Captive Insurance System is a company owning and managing its own insurance, which enables the company to control costs. The term "captive insurer" refers to any subsidiary corporation of a parent company that has been established to provide insurance to either the parent company or its affiliates. As of 2005, Vermont had over 700 licensed captive insurers which makes Vermont the third largest captive insurance company domicile in the world and the largest in the U.S. (Vermont Captive Insurance c. 2005).

In 1981, Vermont passed legislation supplying the suitable regulatory and taxation environment for captive insurance companies. The legislation's purpose was to create a friendly environment for businesses and companies developing captive insurance systems in Vermont (Vermont Captive Insurance c. 2005).

The individual business costs associated with captive insurance in Vermont are found in the application process that, including licensing, initially costs $3,700. However, after gaining State approval, only a $300 annual re-licensing fee is due (Vermont Captive Insurance c. 2005).

Advantages of Captive Insurance

Through the Captive system, companies are able to keep insurance costs low by avoiding inflated premiums of an outside insurance company. They also have access to a wider range of insurance markets than are generally available commercially because they literally create both the supply and demand for the insurance (Captive Insurance Companies 2000).

Another advantage of captive insurance stems from increased cash flow within a company as compared to a traditional, outside insurer where premiums are paid in advance but claims are given out over a longer period of time. In the case of captives, premiums are available for further investment until claims are made to them and the claim may be paid out at an increased rate. (Captive Insurance Companies 2000) Further advantages to Captive Insurance are the reduction of company operation costs, direct access to reinsurance markets at wholesale, greater control within the captive and the ability to better negotiate with underwriters (Vermont Captive Insurance c. 2005).

The state of Vermont has itself benefited from offering captive insurance to companies whose main headquarters are located within the state. A Vermont State Legislative report conducted in 1996 attributed the collection of $8 million in captive premium taxes. (Legislative Fiscal Committee c. 1996) Vermont has licensed over 400 captives since 1996, implying that State revenue has likely only continued to increase as a result of allowing captive insurance (Vermont Captive Insurance c. 2005).

Captive Regulations

Under Vermont law, businesses must comply with a variety of requirements put forth by the State in order to qualify as a captive insurer. These include limiting the types of insurance a company can provide and also to whom the coverage can be offered; both variables are dependant on which type of captive insurance a business uses. Several different classifications of captive insurance exist including pure captive insurance, association captive insurance, and industrial insured captive insurance or as a risk retention group. However, the overwhelming majority of Vermont captive businesses are currently classified as pure captive insurance companies. (Vermont Captive Insurance c. 2005)

All captives must further conform to standards such as submitting annual financial reports to the State, having a yearly independent audit, and notifying the State of any changes to its board of directors or any other executive officers. The state may further require companies to put down a deposit if the commissioner deems it necessary as a result of the financial situation of the company. (Vermont Captive Insurance c. 2005)

Corporate Social Responsibility

Although the United States has no formal definition for Corporate Social Responsibility (CSR), many leaders and organizations have taken it upon themselves to give accurate descriptions as to what a responsible corporation encompasses. One broad definition by the Congressional Human Rights Caucus, defines CSR as pursuing commercial success while still honoring ethical values and respecting people, communities, and the environment. During this caucus, Susan Aaronson, a globally recognized expert on trade policy issues, provided the key detail that these businesses must *voluntarily* want to promote corporate responsibility (Congressional Human Rights Caucus 2005). Combating corruption, and "encouraging corporate philanthropy" are several aspects of CSR according to Lorne W. Craner, the Assistant Secretary of State for Democracy, Human Rights and Labor in the U.S. (Craner 2002). The World Bank defines CSR as "a collection of policies and practices linked to relationship with key stakeholders, values, compliance with legal requirements, and respect for people, communities and the environment…The commitment of business to contribute to sustainable development (World Bank 2002).

In addition, the U.S. state department presents The Award for Corporate Excellence every year based on certain factors compiled by the Chief of Missions of U.S. diplomatic posts that businesses must follow. These factors are:

- Good corporate citizenship
- Provision for a safe and healthy workplace
- Exemplary employment practices
- Environmental protection and practices
- Contribution to the overall growth and development of the local economy
- Implementation of activities that are compatible with local science and technology policies while contributing to the development of in-country innovative capacity compliance with U.S., international and local laws, especially regarding anti-bribery and transparency (U.S. State Department 2003, from: http://www.state.gov/e/eb/rls/othr/25246.htm).

Two examples of companies that have won this award were the Ford Motor Company and the Solar Electric Light Company in 2001. The former initiated an HIV/AIDS program in Africa and the latter provided solar energy to rural villages in Vietnam (Craner 2002).

Promoting Corporate Social Responsibility

At an e-forum held by the World Bank Institute on Corporate Social Responsibility, the size of the role government should play in promoting CSR was debated. Forum participants agreed that there are many benefits to be had from being named a socially responsible corporation. These include, getting a license, drawing more investors, and avoiding a crisis. (World Bank 2002)

One long-term promotion plan is the establishment of socially responsible investment funds, many of which have already been set up. Socially responsible investment (SRI) means that one makes investment decisions with social and environmental concerns in mind. By integrating CSR issues into their "business strategy" they can get these SRI funds and increase their profit (World Bank 2002).

In addition, Oxfam has given four recommendations to the EU on how to promote corporate social responsibility that could apply, on a small scale to the state of Vermont. The first recommendation is to define corporate social responsibility into a formal definition with set guidelines, and principles and establish a "Compliance Panel" that makes sure that those companies with EU contracts or financial guarantees adhere to the human rights laws and policies. The next recommendation is to set up a "contingency fund" which would focus on unintended consequences of business in adversely affected communities. The third recommendation is guaranteeing that the European Investment Bank consistently supports responsible corporations and clearly outlines the qualifications a company must have to gain support from the bank based on social and environmental criteria. The last recommendation is that a "register of blacklisted companies" be set up, which lists which companies have been convicted of corruption. The EU would then classify these companies as ineligible for contracts or awards for a period of three years. (Oxfam International 2002)

The World Bank published a report regarding the best ways governments can promote Corporate Social Responsibility in Europe and Central Asia, which can be applied to state governments in the United States. Basically, businesses agreed that their perceived “loss of competitiveness” and other potential losses could be reduced if the government had concrete, clear and predictable policies and financial incentives to promote social responsibility. Businesses seemed to greatly doubt the government’s policies, and expect that there would be hidden costs and liabilities.

One way to avoid confusion is to set numerical or quantitative objections that can be easily monitored. For example, establish goals regarding “the types of activities; the numbers and types of beneficiaries of these activities; the diversity of businesses involved…and the continuity with which corporate social responsibility practices are used” (The Development Communication Division, The World Bank, p. 27, 2005). The government and policy makers try to alter the actions of corporations to encourage social responsibility by paying extra attention to businesses who are not abiding by the laws and regulation and enforcing penalties to those that don’t; enforcing “tax incentives, technical assistance”, encouraging communication between business and civil society and “raising public and corporate awareness” (p. 28). Another recommendation is combining the public and businesses’ funds to gain more money, exchange ideas to implement social responsibility in the corporations. Finally, raising public awareness of business practices, can promote social responsibility by giving good exposure and praise to the company.

Organizationally, a government can make a separate agency for corporate social responsibility or add it to an existing agency such as one that handles policy implementation. Regardless it seems as though, “developing mandated actions and monitoring compliance and enforcement” would also be financed by the state. Sharing these costs, however with businesses will depend on whether policies are implemented that encourage a joint venture (The Development Communication Division, The World Bank, 2005)

The US Embassy in Prague provided a number of workshops and seminars to community foundations, NGO’s, and businesses with steps to implement corporate social responsibility into their communities and organizations (Embassy Events).

The Commissions European Social Agenda, which is supported by the European Council in Nice, was invited to gather companies to meet with social partners, local authorities, NGO’s, and organizations that handle social services, in order to strengthen social corporate responsibility. They discuss sustainable development and public policy, which are important topic of social corporate responsibility. Public Policy plays a significant role in promoting social corporate responsibility and creating a structure to guarantee that businesses are concerned with social and environmental issues and including them in their activities and guidelines. Also, companies, organizations, and the government look for ways to produce products and services to encourage health and safety. There are ways to record the safety of these products to be able to document and advertise these ‘responsible’ products (European Commission).

Resources

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