



**RISK MANAGEMENT CLUB FOR THE VCS –
FEASIBILITY - MANAGEMENT SUMMARY
JULY 2003**

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MANAGEMENT SUMMARY

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1. INTRODUCTION, OBJECTIVES AND APPROACH

1.1 Charity Logistics invited Z/Yen Limited (Z/Yen) to deliver a feasibility study for a mutual risk management club to provide insurance to the Voluntary and Community Sector (VCS). The study was supported and endorsed by the Active Community Unit of the Home Office, the Charity Finance Directors Group, the Institute of Fundraising and the Association of Chief Executives of Voluntary Organisations. The fieldwork for the review was conducted between March 2003 and May 2003.

1.2 The study's objectives were to determine the answers to three questions related to VCS insurance:

- ◆ Is the VCS a good 'risk' for insurance?
- ◆ Could the VCS work together to help each other in terms of risk management?
- ◆ Could some grouping (or groupings) of the VCS reduce their insurance costs and/or improve their risk management?

1.3 The approach taken in the feasibility study was to survey the current insurance situation within the VCS sector and to conduct a number of interviews with industry experts:

- ◆ 116 VCS organisations completed a questionnaire that explored the structure of the VCS insurance, insurance cost trends, claims records and attitudes to risk management. 73 of these organisations provided complete insurance financial information for 2002/3 and 2003/4;
- ◆ industry expert interviews were conducted with 4 insurance companies (Ecclesiastical, Zurich Insurance, Norwich Union, Royal Sun Alliance), 3 insurance brokers (Scottvale, Marsh, MCIS), 3 insurance mutual management companies (Charles Taylor Consulting, Thomas Miller, Tindall Riley), 2 risk management advisors (Fairweather Risk, Clayton Risk Management), a financial journalist (Mitre Publishing) and the Association of British Insurers (ABI).

2 ISSUES IDENTIFIED BY RESEARCH

2.1 Table 1 shows the total figures for the 73 organisations that completed the survey fully. The organisations have been segmented using the Charity Commission size-by-expenditure categories.

Table 1 - Totals

	"Large"	"Medium"	"Small"	"Very Small"	Total
Classification	>£10m	<£10m & >1£m	<£1m & >£250k	<£250k	
Number of organisations	26	18	13	16	73
Total Expenditure	£1.3bn	£54.6m	£6.7m	£1.2m	£1.3bn
Total Insurance Premiums 2002/3	£11.6m	£779k	£417k	£25k	£12.8m
Total Number of Claims 2002/3	1738	118	4	0	1860

	“Large”	“Medium”	“Small”	“Very Small”	Total
Total Value of Claims 2002/3	£2.2m	£300k	£33k	£0	£2.6m
Total Insurance Premiums 2003/4	£13.7m	£1.0m	£474k	£33k	£15.2m
Total Insurance Premium Increase 2002/3 to 2003/4	£2.1m	£239k	£57k	£8k	£2.4m

2.2 Table 2 shows the average profile of the 73 organisations that completed the survey fully.

Table 2 - Averages

	“Large”	“Medium”	“Small”	“Very Small”	Average
Classification	>£10m	<£10m & >1£m	<£1m & >£250k	<£250k	
Expenditure	£46.8m	£3.0m	£526k	£75k	£14.6m
Employees	1,189	85	43	3	370
Insurance Premium 2002/3	£447,209	£43,274	£32,053	£1,581	£176,005
Number of Claims 2002/3	67	7	Less than 1	0	25
Value of Claims 2002/3	£86,203	£16,641	£2,533	£0	£35,257
Insurance Premium 2003/4	£527,547	£56,529	£36,460	£2,071	£208,779
Insurance Premium Increase	£80,338	£13,255	£4,407	£489	£32,774
Ratio - Claims 2002/3 to Premium 2002/3	19.3%	38.4%	7.9%	0.0%	20.0%
Insurance Premium Increase 2002/3 to 2003/4	18.0%	30.6%	13.8%	30.9%	18.6%

2.3 89% of the VCS have experienced an insurance premium increase for 2003/4. 82% of the VCS were informed that the prevailing reason for this increase was “market conditions” rather than a VCS specific risk.

2.4 There is evidence that the VCS receive inconsistent pricing. For instance, the 18 care-related VCS in the survey had premium increases in 2003/4 ranging from -6% to 145%. Some of the VCS with low price increases had a high claims-to-premium ratio. The fact that price increases vary widely and unpredictably infers that there is no consistent method of assessing and pricing VCS insurance.

2.5 Several expert interviewees stated that care and counselling services are seen as a high risk for claims on the Employer’s and Public Liability policies regardless of whether the services are provided by a VCS or not. It would appear that the VCS organisations that provide care and counselling are rated as high risk, particularly for Employer’s and Public Liability cover, especially if they provide services to “vulnerable” groups such as children or the disabled. In our survey 18% of the VCS organisations had been unable to get the full insurance cover they required. Of that 18%, 35% work with children/young people whereas only 18% in the whole sample work with children/young people.

2.6 Several expert interviewees stated that some of the VCS are perceived by insurers as too small to justify the cost of a risk assessment visit to understand the organisation better. 65% of the VCS organisations that are unable to get the full insurance cover they require are “small” or “very small” whereas only 45% of the whole samples are “small” or “very small”. It appears that “small” or “very small” VCS organisations are more likely to be unable to get the full insurance cover they require.

2.7 According to the expert interviews, a claims-to-premium ratio of between 50% and 60% will sustain an appropriately provisioned, profitable insurance business. If the claims-to-premium ratio is less than 50%, then the business will be even more profitable for the insurer. The claims-to-premium ratio during 2002/3 for the VCS that participated fully in the survey was an average of 20% across all categories of insurance. This indicates that the VCS could be a profitable business for insurers.

2.8 The ABI provided figures for certain classes of insurance that their members provide. The average claims-to-premium ratio for ABI members in 2001 was 118% for Employer’s Liability insurance and 85% for all Liability insurance excluding Employer’s Liability insurance. On the basis of these averages and the averages from our research, it would appear that VCS claims ratios are significantly lower than the market generally for these types of insurance. If the survey returns are valid, then the VCS are more profitable than insurance companies may realise.

2.9 Whilst some of the industry experts agreed that many of the VCS managed their insurance risks well, it appears that better risk management tends not to reduce the price of insurance and hence its affordability in this sector. 65% of the VCS have carried out an audit of risks, 38% have adopted additional security measures and 25% have developed a risk manual. No relationship was found between risk management actions and insurance premium price increases.

2.10 Of the 284 policies held by the 116 survey participants, six insurance companies held 56%: Royal Sun Alliance 17%, Norwich Union 13%, Ecclesiastical 6%, Zurich 6%, Lloyds 6%, AIG 6%. This concentration might result in a limited range of insurance for the VCS.

2.11 Of the 109 brokers used by the 116 survey participants, six brokers held 38%: AON 14%, Marsh 6%, Perkins Slade 6%, MCIS 4%, Willis 4%, Heath Lambert 4%. 58% of the VCS state that their broker has helped to negotiate the best rates on their behalf and 77% of the VCS renew with advice from their broker. 16% of the VCS do not use an insurance broker.

2.12 There is a tendency for some of the VCS to renew without negotiation. Whilst none of the “large” VCS renew their insurance without negotiation, 35% of the “very small” survey participants do not negotiate or consider alternative insurance suppliers on renewal.

3 OPTIONS FOR ACTION THAT MIGHT REDUCE VCS INSURANCE COSTS

3.1 VCS organisations could negotiate a lower insurance premium if they retained a higher proportion of any claim. A lower insurance premium could be negotiated by raising the policy excess or by putting a limit on the level of cover. 56% of the VCS organisations surveyed have yet to consider raising their policy excess and 82% have not reduced the level of their cover.

3.2 The VCS could use brokers more effectively to “educate” insurers on the true level of risk and to explain the risk management that they undertake. One broker who focuses exclusively on the VCS sector stated that they have obtained cover for all of their clients at competitive levels of premium increase.

3.3 Some joint activities by the VCS could reduce insurance costs. 77% are willing to share risk management best practice, 74% are interested in buying insurance as a group and 68% were interested in developing group insurance for the VCS. But 31% of the survey participants say that there are some VCS organisations that they would not be willing to work with.

3.4 According to experts, if similar VCS organisations aggregated their premiums so that their combined purchasing represented an aggregate premium of £500,000 or more, then it is possible that they could get lower premium increases. This would require dozens of “medium” or “small” VCS or several hundred “very small” VCS to aggregate their purchasing. The average premium increase in 2002/3 was 17.96% for the “large” VCS organisations and approximately 30% for the “medium” and “very small” VCS organisations.

3.5 If the VCS undertook a regular VCS insurance benchmark, it is possible that inconsistent pricing could be identified and through negotiation, reduced. Such a benchmark could also support negotiation with insurers at the time of renewal of cover and provide evidence of sector wide change in insurance or broker behaviour.

3.6 There is a potential role for the Government or the VCS associations to set standards of organisational behaviour so that better run VCS organisations could be rated as representing a better risk. Government might even be encouraged to directly support VCS insurance in the same way as the DTI TRADESMEN scheme, which delivers a 20% discount on liability insurance to good quality builders.

3.7 The VCS could bulk buy with a single insurer in return for a share of the profits on their insurance premiums. That “share of profits” might be returned through lower premiums or be used to create a fund over time with the insurer.

3.8 The VCS could form a mutual insurance club. Risk management “clubs” are used in a number of industry sectors to underpin world-class standards with financial reward for risk management. Mutual clubs need a critical mass of annual premium to cover claims, costs and to build a fund for the future. Experts suggest that the minimum size would be a total annual premium of at least £5m of cover from similar VCS organisations. This would require the combined purchasing from ten or more “large” VCS organisations, one hundred or more

“medium” or “small” VCS organisations, five hundred or more “very small” VCS organisations or some equivalent combination of different sized VCS organisations. In particular, long tail liabilities (such as health and abuse claims) need to be provided for over time. It is possible that mutual clubs could deliver insurances at savings of around 20% over conventional insurance.

4 RECOMMENDATIONS

4.1 Z/Yen recommends that VCS organisations undertake a three-phase approach to their insurance. If a “critical mass” of VCS organisations were committed to joint action then it may be possible to undertake the later phases directly.

4.2 Phase 1

4.2.1 Step 1 - Review current insurance structure

- ◆ Negotiate renewal rates rather than allow un-negotiated renewal;
- ◆ Review current level of cover and level of excess on policies to see if policies can be changed to decrease insurance premiums;
- ◆ Consider moving business to a specialist VCS insurance broker;
- ◆ Consider a “badged” insurance scheme by providing access to a membership (e.g. bulk discount for members).

4.2.2 Step 2 - Share information with other similar VCS organisations

- ◆ Benchmark insurance costs and claims, consolidate reporting;
- ◆ Share best practice in terms of risk management, broker behaviour and policy negotiation;
- ◆ Use the aggregate VCS information to raise the profile of inconsistent pricing and to pressure support from insurance providers and Government.

4.2.3 Step 3 - Group purchasing with other similar VCS organisations through specialist brokers

- ◆ Aggregate insurance purchasing through a specialist VCS insurance broker. Similar VCS organisations could combine their premiums to aggregate to more than £500,000. With such a large aggregated premium the broker will be able to negotiate a more competitive rate, provided the claims history is good and risk management behaviour is consistently applied.
- ◆ Use specialist brokers to “educate” the insurance market and get insurers to recognise that the VCS can be a better and more profitable risk.

4.3 If enough VCS organisations undertake Phase 1 actions then there may be a “critical mass” of organisations to undertake Phase 2 as follows. Alternatively, if a “critical mass” of VCS organisations were committed to joint action then it may be possible to undertake Phase 2 directly.

4.4 Phase 2

Group purchasing with other similar VCS organisations negotiated with a specific insurer

- ◆ A specialist broker who has a sufficient number of similar VCS organisations as clients could represent the VCS organisation for this group purchasing;
- ◆ Aggregate group premium income would need to approach the critical mass necessary for the formation of a mutual (£5m) in order to attract the interest of an insurance company.

4.5 If enough VCS organisations undertake Phase 2 actions then there may be a “critical mass” of organisations to undertake Phase 3 as follows. Alternatively, if a “critical mass” of VCS organisations commit to joint action, it may be possible to undertake Phase 3 directly.

4.6 Phase 3

Formation of mutual risk management structure with other similar VCS organisations

- ◆ After a successful track record of purchasing as a group it might be possible to “capture” the insurance company profit margin by forming a mutual insurance company;
- ◆ The aggregate group premium income would need to exceed the critical mass of £5m necessary for the formation of a mutual and would ideally be above £10m;
- ◆ Phases 1 and 2 could have the effect of “training” VCS organisations to work together and manage risks proactively, which increases the likelihood of forming a successful mutual;
- ◆ Government endorsement and/or incentives for Phases 2 and 3 could increase the likelihood of success and the speed of progress through the phases.

4.7 These recommendations will require VCS organisations to work together; they could be facilitated by one or more of the sector organisations such as Charity Logistics, the Charity Finance Director’s Group, the Institute of Fundraising, the Association of Chief Executives of Voluntary Organisations or the Active Community Unit of the Home Office. In particular, the Government can help to facilitate phases 2 and 3.

5 ILLUSTRATION OF THE LEVEL OF EFFORT AND LEVEL OF RETURN FOR THE PHASED RECOMMENDATIONS

