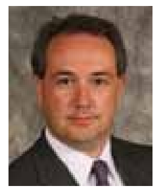
Protecting Your Credit Union

A More Strategic Approach

2013

As a credit union, you are strategic in everything you do. Shouldn't your approach to risk/insurance be the same?



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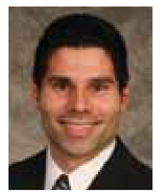

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Why do you buy directors and officers insurance? Or for that matter, any insurance? While it seems like a simple question, it is one that is often overlooked in the insurance risk management process. Understanding the answers can help shed light on management's perceived risk and concerns, as well as its preferences and tolerances. It also can radically change how credit unions look at their insurance programs, what they buy, and how it is managed.

Applying a strategic decision-making process to risk is becoming more important with heightened exposures and increased regulatory scrutiny. We see more sophisticated credit unions transition from a procurement mentality to one of strategic planning. This can help control insurance costs, and ensures that the credit union has consciously structured its programs to manage its risk exposure in a manner that is consistent with its business strategy and risk tolerances.

Conducting a strategic insurance planning process should be applied to most forms of insurance (for example, directors and officers, bond, property and casualty, identity theft). We even recommend this strategic process for your suite of employee benefits insurance programs (such as, health insurance, life insurance, accidental death and dismemberment) and even retirement plans.

The basic approach is the same: What are your concerns? What are you trying to do? Why? To what level? To help our clients answer these questions, we developed a three-step risk planning methodology:

Risk Planning Methodology	
	1. Identification of risk exposure. 2. Assessment of the risk and action-planning each item. 3. Custom-designed risk solutions, including insurance programs, to meet your specific exposures and preferences.

1. Identification of risk exposure:

- Operational—business interruption, protection and retention of key assets and people.
- Reputational—brand impact and member perception and satisfaction.
- Financial loss of income, demands for damages, data breach notification costs.

Each credit union has a unique risk footprint. This can be influenced by several factors such as: loans and services offered (online banking, trust services), ownership in a CUSO, membership base, number of branches and its location, board members and employee demographics.

The first step is helping credit unions think through all the areas that could expose them to risk and what this exposure could mean to their operations, reputation and financial health. This can often be an eye-opening process and can bring insurance to life by helping management and board members see more clearly all the things that insurance could possibly apply to.

Fully understanding your credit union's areas of risk takes you to the assessment and planning step of the process.

2. Assessment of the risk and action-planning each item:

- Estimate the impact and likelihood of the risk.
- Determine management risk tolerance and preferences: risk adverse, comfortable with known risk, frequency versus severity, etc.
- Develop plan for each risk: retain or transfer, insure and to what level.

Insurance is not always the answer. Only with a comprehensive understanding of your risk exposure and the potential impact to your credit union can you then strategically outline the most appropriate method to protect your credit union. Typically, risks fall into one of several buckets:

- Not appropriate for insurance—i.e., business risk items.
- Contractually transfer the risk through alternative vehicles (contracts, outsource).
- Retain all or a portion of the risk.
- Transfer the risk through insurance.

> Each credit union has a unique risk footprint that we help it understand.

Determining where your specific exposures fall will provide the raw input for what your insurance programs should ultimately look like and be tailored around.

Developing a plan leads to the design phase of the process.

3. Custom-designed risk solutions, including insurance programs, to meet your specific exposures and preferences:
   - Examine existing programs to evaluate how effectively they serve their purpose.
   - Benchmark versus other credit unions or financial institutions and what is currently available in the marketplace.
   - Negotiate specific policy language, terms, conditions and retentions, not just limits and premiums.

Conducting a thorough strategic insurance planning process with an independent expert to help you custom tailor your insurance program will position your credit union to be more confident that it has insured the risks it is most concerned about; at appropriate levels; and has applied its premium spend more effectively to achieve its strategic goals.

The following three case studies highlight how this strategic planning process aided other credit unions in creating tailored solutions for specific needs.

CASE STUDY #1: DOES MY DIRECTORS AND OFFICERS COVERAGE PROTECT MY BOARD/ MANAGEMENT/CREDIT UNION SUFFICIENTLY?

1. Identification of risk exposure:

Responding to questions and concerns from the Board, the credit union engaged Lockton to assess the quality of its current program and appropriateness.

2. Assessment of risk exposure:

The credit union used the industry standard policy form, but had never had an insurance expert help it fully examine the specific terms and coverages negotiated. The result was the policy had several restrictions and coverage exclusions that were problematic:

A. Claims against the credit union (entity) were not covered.

B. Regulatory actions were not covered.

C. No coverage for defense costs for certain conduct allegations (dishonest acts, improper gains).

D. No ability for the credit union to choose its own defense counsel.

E. No coverage or defense would remain for the innocent parties due to the actions of the guilty party.

F. Definition of a claim would not include criminal actions or civil money penalties.

G. Insurance company was allowed to cancel coverage during the policy term for any reason.

The policy had reasonable limits and premiums as compared to their peers. However, because of these restrictions, the credit union deemed the coverage was inadequate and poor value for the premium.

3. Custom-designed risk solutions:

Lockton worked with the credit union to develop new coverage that provided insurance for each of the deficient areas. Also, Lockton redesigned the policy limits to structure an appropriate amount of coverage for each of its three constituencies (directors, officers, and the entity), based upon its needs and preferences. It resulted in a program that provided more robust coverage.

> “Never had an insurance expert help it fully examine the specific terms and coverages negotiated. The result was the policy had several restrictions and coverage exclusions that were problematic.”

CASE STUDY #2: MANAGING EMPLOYEE BENEFITS AND RETIREMENT PROGRAMS TO RESPOND TO GROWING COMPLIANCE CONCERNS

1. Identification of risk exposure:

A. Healthcare legislation created compliance concerns and challenges. The credit union client had limited internal bandwidth to stay on top of evolving regulations and provided a strategic plan to address these needs.

B. Retirement programs required independent analysis of fund performance and fee reasonableness. The credit union received this review from the vendor, which the Department of Labor guidelines stipulate is not considered independent.

2. Assessment of risk exposure:

A. Healthcare: New regulations imposing changes in 2011, 2012, 2013, 2014 and 2018. How do the employee benefit programs need to be amended to respond to these regulations? What is the cost impact and how does the credit union provide long-term budget analyses around these changes?

B. Retirement: The credit union lacks internal bandwidth and expertise to conduct sophisticated fund performance and fee reasonableness reviews, so it needed an independent source.

3. Custom-designed risk solutions:

A. Healthcare: Lockton worked with the client to produce a detailed review of how healthcare legislation will impact the client. We then developed a three-year action plan to respond to the specific components and regulations so the credit union would be compliant.

B. Retirement: Lockton worked with the credit union client as an independent consultant on all retirement plans—401(k), pension, and the 457(b) nonqualified plan to comply with Department of Labor guidelines.

CASE STUDY #3: PRIVACY THEFT RISK

1. Identification of risk exposure:

A credit union, with more than 46,000 members, stores personal identifiable information, including salaries, Social Security numbers, address and work history. Exposure to the loss or compromise of this data exists whether the credit union stores the data or uses a third party.

2. Assessment of risk exposure:

A breach of credit union information results in notification costs to affected members—approximately $200 per member. No insurance and/or contractual transfer mechanism is in place, leaving the credit union with an unfunded and uninsured potential liability of $9.2 million. Traditional liability and bond insurance would not cover this type of loss, and even some cyber policies restrict coverage to only $250,000 for notification costs.

3. Custom-designed risk solutions:

Lockton worked with the credit union and technology vendors to modify contracts to provide some contractual risk transfer mechanism. Then, Lockton evaluated the full exposure to risk for insurance purposes, and designed a tailored insurance product to respond to the remaining notification cost liability and the vicarious liability from outsourcing.

> “Traditional liability and bond insurance would not cover this loss.”

> Develop the program that is right for you, rather than settling for the generic "off-the–shelf" offering.

Takeaways

To conclude, moving to a strategic planning process will help credit unions identify and quantify their own risk footprint and have a better discussion on how to manage this risk. This will allow you to develop the program that is right for you, rather than settling for the generic "off-the-shelf" offering; thus, tailoring your premium spend more effectively and in a way most appropriate for your credit union.

It is important to know that you have choices, and you are not alone. By partnering with an independent broker with a dedicated and proven credit union practice, you gain a better understanding of your specific risks and how to best manage them. You also gain access to an invaluable guide to help obtain and compare options from the entire insurance market, resulting in greater assurance that you have a superior product, tailored to fit your risk profile and preferences.

Our Mission

To be the worldwide value and service leader in
insurance brokerage, employee benefits, and risk management

Our Goal

To be the best place to do business and to work

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