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INSURING YOUR BUSINESS

FALL 2010

HOW MUCH LIABILITY INSURANCE IS RIGHT FOR YOUR TRUCKING FLEET?

By Michael R. Kelley

The Federal Motor Carrier Safety Regulations require that commercial trucks carry a liability insurance policy of a certain minimum amount, in most cases $1 million. But, is this minimum coverage right for your trucking fleet? If the minimum is not right for your fleet, how much liability insurance coverage should you have?

There is no one answer that covers all trucking fleets. The requisite amount of insurance is different for a single owner-operator than it is for a fleet of several hundred trucks. Nonetheless, there are common factors that every trucking company should consider in determining the amount of liability insurance coverage that it needs.

The factors that you should consider are:

- **Past claims history**. You should look at your past claims history over a ten year period. If you are unfamiliar with the claims history, or do not remember the specifics, ask your insurance broker or carrier. As with financial investing, past performance is no guarantee of future results, but it does provide a base of information on which to build.

- **Nature and scope of risks**. For trucking companies, the primary liability risk is an accident involving third parties. An accident can take the form of anything from a minor injury to a single third party to a multiple car pile-up with numerous serious injuries and deaths. Virtually every trucking company faces these potential risks. A worst-case scenario (involving multiple vehicles and multiple serious injuries and deaths) could involve claims of $10,000,000 or more.

- **Company assets**. Generally speaking, the greater the assets of a company that would be subject to execution, the more insurance coverage that company should have. By way of example, lets assume that one of your trucks is involved in an accident in which two people are killed. We will further assume that each of the claims is valued at $3,000,000, that your company has the minimum $1,000,000 in insurance coverage, and that your company owns assets of $5,000,000. Under this

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PREMIUM SAVINGS NOW, CAN COST YOU LATER

By Charles T. Young, Jr.

In these difficult economic times, many companies have acted to reduce their insurance costs by participating in trade association programs or self-insuring in ways intended to achieve premium savings. These savings, however, can sometimes be difficult to verify. Moreover, the insurance arrangements are not always free from risk, and premium savings can rapidly dissipate if litigation or other problems ensue.

Trade groups often form relationships with insurers and brokers in an effort to provide a benefit to their members. These relationships are very common, and they can be a valuable asset to the group's members. For instance, the trade group's members might receive a discount if they participate in, and purchase insurance through, the group's program. The concept is straightforward, but the reality can become quite complex.

A business should take a close look at the premium savings that will realistically be achieved from participating in such programs. In many instances, the complexity of the programs obscure whether premium savings will occur. For instance, insurers commonly market programs based on the dividends that will be paid to participants. These dividends are paid at the discretion of the insurer, and the savings are therefore subject to debate. It is also common for insurers to impose restrictions on the dividends that may be paid, and the restrictions may be "buried" beneath several layers of documentation. A business should carefully examine the program documentation and consider whether the potential savings justify participation.

Risk retention groups ("RRGs") are another mechanism for achieving premium savings and other benefits. Essentially, an RRG is a form of self-insurance in which a group of companies provide their own insurance by establishing their own premiums and reserves. RRGs work well, and they are certainly an option for many companies. They are not, however, a cure-all. In the event of a serious claim, an RRG member will likely pay more than a business insured through a traditional insurer. RRG members need to closely monitor who they admit to the group and carefully scrutinize the members' claims histories. It is important for a company to be actively involved. If a business cannot (or will not) be actively involved, then an RRG may not be a good option.

RRGs have also begun to act more like traditional insurers in that they market their products to non-members through a trade association or other outlet. These non-members have no control over the RRG's decision-making or operations. While an RRG may be a great choice for its members, the RRG may not be such a great option for non-members. A non-member will not have control over the admission of new members or setting of premiums. It may, therefore, suffer adverse consequences because of decisions made by others.

RRGs differ from traditional insurers in many ways. For example, a company purchasing insurance through a traditional carrier will be covered by the state's guaranty

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scenario, if your company was found liable for the accident, $5,000,000 of your company's assets (over and above the insurance policy) would be subject to being executed upon by a plaintiff in a lawsuit. If your company does not have enough liability insurance to cover a catastrophic accident ($10,000,000 or more), it should at least have enough insurance coverage to protect the assets of the company.

- **Consider the jurisdiction(s) in which you do business**. The jurisdiction in which you do business affects your liability exposure. For instance, Maryland has a cap on damages for pain and suffering. Pennsylvania does not. If you are a trucking company doing business exclusively in the state of Maryland, your liability coverage requirements would be less than if you do business in multiple states, or even just do business in Pennsylvania. Check with your attorney concerning your liability exposure in the jurisdictions in which you conduct business.

- **Your comfort level with risk**. Ultimately, the amount of insurance coverage that your company should have, in excess of the minimum amount, depends upon your company's comfort level with assuming risk. If you want to make sure that all of your company's assets are protected and that you have enough insurance coverage for even a worst-case accident, you should have a significant amount of insurance coverage above the minimum required by law. Some companies are more comfortable assuming some risk in the event of an accident, and therefore are willing to trade that risk in return for lower insurance premiums. The bottom line is that you should be aware of the factors involved in determining the appropriate amount of insurance coverage when determining your level of comfort with that risk.

There is no one answer for all trucking companies to the question of how much insurance coverage is necessary. The above factors should be considered by all companies in reaching that conclusion. You should also work with your insurance broker and insurance counsel to help determine the appropriate level of insurance coverage that is right for your company. ■

Michael R. Kelley is Chair of the Insurance Litigation and Counseling group and also practices in the Litigation group.
717.237.5322 / *mkelley@mwn.com*

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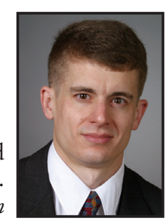
association in the event the insurer becomes insolvent. A company purchasing insurance through an RRG will not be covered by the guaranty association. The policy forms issued by a traditional insurer will also be scrutinized by the state's insurance department. The policy forms issued by an RRG, on the other hand, are often not subject to such scrutiny. These may be perfectly acceptable trade-offs for an RRG member. For a non-member, the calculus may be different.

Insurance is a highly regulated field, and the complexity of alternative insurance arrangements can create problems for companies seeking premium savings. For example, a company or trade association may expect to receive some sort of benefit or payment which is not fully evident from a review of the program's literature. However, Pennsylvania law prohibits the payment of undisclosed "rebates" of any kind and provides for severe sanctions. Rebates include all manner of inducements or benefits. It is therefore important that any rebate, discount, or other benefit be clearly disclosed in the policies issued.

The search for premium savings may also lead a company or trade group to engage in activities resembling those of an insurance broker. Generally, a company can perform many insurance related functions without obtaining a broker license. However, a good broker can bring real value to a transaction and should not be overlooked. Furthermore, if a company or trade group receives a fee or other benefit tied to the sale of insurance, then it is potentially acting as an unlicensed broker or "producer." It will therefore need to obtain a producer license, and failure to obtain the required license can result in criminal penalties.

Alternative insurance arrangements can result in substantial savings, but businesses and their trade groups need to have realistic expectations. They should be as informed as possible about the actual benefits to be achieved through these arrangements. The promises of substantial savings may not bear out under close scrutiny. Moreover, the sale of insurance is a highly regulated activity. If a business or its trade group is unaware of the regulatory hurdles, then the expected premium savings may rapidly dissipate in a cloud of litigation, fines, and penalties. ■



Charles T. Young, Jr. practices in the Litigation and Insurance Litigation and Counseling practice groups.
717.237.5397 / *cyoung@mwn.com*

Insurance Litigation & Counseling Group

Michael R. Kelley, Chair
717.237.5322/mkelley@mwn.com

Richard H. Friedman
717.237.5469/rfriedman@mwn.com

Jonathan H. Rudd
717.237.5405/jrudd@mwn.com

Bruce R. Spicer
717.237.5331/bspicer@mwn.com

Dana M. Windisch
717.237.5457/dwindisch@mwn.com

Charles T. Young, Jr.
717.237.5397/cyoung@mwn.com