

# The View from Level VII™

## RISK MANAGEMENT

### *The "Kitchen Sink" Quarter*

I'll bet you, as an insurance consumer, never thought the kitchen sink would play a crucial role in the amount of premium you pay. Well, it does, quite a bit in fact.

Insurance company accountants display an unusually good sense of humor, (at least from their standpoint), when they dub the last quarter of their fiscal year as the "kitchen sink" quarter. Kitchen sink accounting allows insurance companies to maximize rate increases in the next fiscal year.

Here's how the formula works: total all paid losses (even though the checks may not be cut until next year), add in reserves for reported losses and inflate to the max, pull a big number out of the sky for what are called "incurred but not reported losses", stir in some helpful trending and total.

Losses must exceed earned premium. If losses do not adequately exceed premium, throw in the kitchen sink before going to the regulators to plead for increases in rates. Finally, collude with the marketing guys to come up with a story that will seem at least a little plausible when announcing outrageous increases to clients. One last thing, investment portfolio gains to reduce a loss ratio must never be credited.

How is that for what the property & casualty insurance industry calls standard accounting practice.

**ERMI**, with its Fortune 500 experience, consults with firms of all sizes in the area of risk management.

**Roger Wilcox**  
Enterprise Risk Management, Inc.  
[www.ERMIONline.com](http://www.ERMIONline.com)

*In this and/or future issues you will find short, yet meaningful articles on:*

- Human Resources
- Risk Management
- Executive Compensation
  - Executive Benefits
  - Employee Benefits
- Private Wealth Planning
  - Business Succession

## EMPLOYEE BENEFITS

### *STD Insurance - Time for a Checkup?*

Short Term Disability insurance (STD) is an important but often overlooked employee benefit. This insurance provides income replacement for non-occupational illnesses or injuries. Most employers in New York State are required to provide New York DBL benefits for non-occupational illnesses or injuries, but the maximum required DBL benefit is only \$170 per week.

Because the required DBL benefit is so low, some employees will try to treat any disability as work-related so that they can receive the significantly higher Workers Compensation benefits. Unfortunately, these "non-occupational" Workers Compensation claims can be expensive for employers.

STD insurance can benefit both employers and employees, and following are some key features of STD insurance programs:

- Benefit levels are normally 50% or 60% of pay.
- Maximum weekly benefits range from \$350 to \$1,000.
- Benefits are normally paid for either 6 months or 12 months.
- Benefits payable are integrated with state DBL benefits to prevent over-insurance and to reduce premium costs.
- Employers normally pay only a small portion of the premiums for these programs, and these plans succeed even if participating employees pay 100% of the premiums.

Please contact us if you have any questions regarding Short Term Disability insurance programs.

Emphasizing *personal service, creative ideas, and positive results*, **Benefits Advantage, Inc.** has 30 years experience providing consulting and insurance brokerage services for all types of employee benefits programs.

**Arthur Georger CLU, CEBS**  
Benefits Advantage, Inc.  
[www.BenefitsAdvantageInc.com](http://www.BenefitsAdvantageInc.com)

## EXECUTIVE COMPENSATION

### *"Golden Parachutes"*

More popularly known as "Golden Parachutes", Change-in-Control Agreements ("CIC's") detail severance compensation (and often an array of other benefits) to executives in the event of their termination as a result of a change in control.

Increasingly, during the frenetic acquisition era of the 1990's, CIC's became the norm in public companies. CIC's have become more of an issue in closely held companies as well, as they too seek well qualified executives, to complement or replace family members or partners.

CIC's can 'stand alone', or alternatively be integrated into an overall Employment Agreement.

Key features include:

- Severance compensation
- Stock (or stock-related) awards
- Other benefits (insurances, retirement plans, auto & club allowances, etc.)
- Excise tax (potential federal tax related to "excess" parachute payments)
- Definition of the "trigger event" (voluntary, involuntary termination, etc.)
- Litigation expenses

Each feature needs very thorough consideration, balancing the perspectives of covered executives on the one hand, and the shareholder(s), on the other. Business factors, competitive practices, HR and legal aspects must all be carefully weighed.

Along with protection upon termination, recognition of contributions executives have made to increasing company value is an additionally critical element in developing CIC's. Of course, creation of value should also be rewarded through a long-term incentive plan...but more on that another time.

**Harman & Associates** has Fortune 500 experience, which provides knowledge and hands on experience to assist private and public companies with specific compensation planning needs.

**Ray Harman**  
Harman & Associates  
[www.Harman-Assoc.com](http://www.Harman-Assoc.com)

# The View from Level VII™

## HUMAN RESOURCES

### ADA

A Manager with BellSouth Mobility failed to convince a federal judge that her acute hemorrhoid condition constituted a protected disability under the Americans with Disability Act (ADA).

Charlotte suffered from serious hemorrhoids, for which she underwent several operations. After her final surgery, her physician placed no restrictions on Charlotte other than a request that the company allow her additional bathroom breaks.

After returning to work, Charlotte alleged her supervisor began holding her to a higher work standard than other managers and was gathering evidence to justify her termination. BellSouth asserted she was a poor performer and followed a well-documented progressive disciplinary procedure before firing her.

Charlotte filed suit under the ADA, claiming her acute hemorrhoid condition was a disability because it substantially limited her in the major life activities of walking, standing, sitting, lifting, eating and drinking, among other people.

“To characterize such a common malady as hemorrhoids, even sever hemorrhoids, as a disability would thwart the purpose of the ADA,” the court said granting the employer’s motion for summary judgment. Charlotte was heard to say she felt that the entire experience was a “pain”; no if ands or buts about that!

Knowing your rights and responsibilities as an employer and employee is crucial. We can help.

**HR Professional Consultants, Inc.** offers human resource services and outsourcing for businesses of various sizes.

**Jim Chwojdak**

**HR Professional Consultants, Inc.**

[www.HRProfessionalConsultants.com](http://www.HRProfessionalConsultants.com)

**Visit our website:**  
[www.LevelVIICompanies.com](http://www.LevelVIICompanies.com)

## EXECUTIVE BENEFITS

### 2002, Tough Year at the Top

2002 was a challenging year for Executives and Executive Benefits Planning. Many scandals and scoundrels brought proper attention to addressing compensation and benefits abuses by those who could. Nonetheless, compensation and benefits remain crucial to attracting, retaining and rewarding many fine people who take charge of our companies and drive our economy. Here’s a glance at an executive benefit plan that went right this year:

**Facts:** Building off several long-term benefit components designed and implemented as elements of his compensation package, CEO asked what type of long-term incentive plan might best fit his senior group of five executives.

**Issues:** The issues faced in addressing CEO’s request were: 1) a benefit equivalent of 60% of pay at retirement; 2) unfettered access for executive deferrals, yet golden handcuffs on Company contributions; 3) executive excess deferrals (beyond qualified plan limitations); 4) executive management of own accounts (like the qualified 401(k) plan); and lastly; 5) cost effective asset to balance this liability.

**Solution:** A Nonqualified Security Option Plan. This modern plan is a nonqualified stock option plan, with characteristics of traditional deferred compensation.

To meet the 60% obligation, the design -

based on age, compensation, pay increases & qualified plan offsets – conversion provided that Company could contribute 18.86% (on average) of annually compensation into the plan for the 5 executives. This simplified formula avoided the potential inequities, as well as the administration and accounting complexities of a traditional (one could argue outdated) Defined Benefit plan design.

Today’s technology allowed for web-centric plan installation and administration. The Company administrator may too monitor and manage on-line, mirroring plan and informal funding valuations to appropriately reflect P&L impact.

**Results:** CEO’s Company now provides a progressive, cost effective plan where, beyond the vesting, the executives control and manage their retirement destiny. Empowered executives make happy and productive executives!

**Weir Financial Resources, LLC** is a financial advisory firm offering information, ideas and solutions in Executive Benefits, Business Succession and Private Wealth Planning.

**Jonathan D. Weir, JD**

**Weir Financial Resources, LLC**

[www.WeirResources.com](http://www.WeirResources.com)

### Who are the Level VII™ Companies?

This is the third issue of *The View from Level VII™*, a bi-monthly forum for valuable information and ideas from some of the top business and financial services professionals around. *The View’s* contributors, the **Level VII™ Companies** is an *alliance of business professionals*, who have chosen to share some of their 150 years of experience and complement of talents in business, law, accounting, finance, insurance and investments.

Through *The View*, we are committed to educating our clients and community by bringing timely and accurate information on a variety of business and financial topics. It is our hope that this broad yet incisive source of information, presented in a quick read format, becomes one that the business and professional community will pause to look at in their increasingly busy day.

For more information about us, topics from *The View*, as well as requests or recommendations, please contact us via our website: [www.LevelVIICompanies.com](http://www.LevelVIICompanies.com). Thank you for your time and interest.

