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Improving Liquidity During and After the Pandemic

Beyond its effect on people, the continuing COVID-19 pandemic has had severe effects on the US and global economies. Maintaining liquidity can act as a bridge until economic activity improves, and a number of insurance and risk management strategies can enable that process.

Cash Flow Challenges

Since the pandemic began, businesses have had to contend with volatile financial markets and uncertainty about their current and future revenues and cash flow. With worries about a potential recession growing, many businesses have taken steps to preserve cash — including laying off or furloughing employees and shutting down production — while exploring potential lines of credit and other ways to maintain liquidity. The White House, Congress, and the Federal Reserve have also introduced a major stimulus package, lowered interest rates, and taken other measures to ease companies' pain and ensure capital is readily available.

But adverse effects and uncertainty for businesses will likely persist for some time — with the worst possibly still to come — which underscores how important it is for businesses to preserve cash. In addition to any actions they may have taken so far, busifall in the short-term — as fewer people are working and social distancing measures remain in place — injury rates may increase for some. And employers of all types may experience delays in key processes and the resolution of existing claims, during which time injured employees will continue to collect benefits.

Outstanding liabilities associated with aging inventories of open workers' compensation claims can significantly reduce the amount of working capital — both short- and long-term — that is available to companies. Settling these claims proactively, however, can help employers improve their balance sheets given uncertainty about the post-COVID-19 economic environment.

A strategic approach to closing legacy claims can enable

Replacing Letters of Credit With Surety Bonds

As businesses face higher financing costs, limited access to credit facilities, and falling counterparty value, surety bonds represent a viable means for posting collateral, and an attractive alternative to bank letters of credit (LOCs).

Unlike an LOC, a surety bond does not count against a company's overall borrowing capacity, nor is its pricing tied to interest rate fluctuations. This means that surety bonds can be more cost-effective than LOCs and can enable principals to free up capital and credit for other, more productive uses. They can also allow principals to avoid being overly reliant on the relatively small group of banks that constitute much of the market for LOCs.

Businesses are increasingly using surety bonds to meet a range of collateral commitments. These include posting security for large leases, meeting court demands while appealing adverse rulings, and satisfying requirements for self-insured workers' compensation programs and other forms of insurance coverage.

Financing Premium Payments

Preserving and strategically deploying capital is vital to a business's success at any time, regardless of market conditions, but it is critically important now. Premium financing can help businesses to preserve working capital that would otherwise be used to pay commercial insurance premiums.

In most insurance transactions, a buyer makes a single upfront premium payment — or pays a majority of the premium upfront — in return for coverage over the next year. A large upfront payment can prevent a business from meeting other critical and cash-intensive obligations, including payroll and supply chain expenditures, at the time a policy incepts or in the future.

Premium finance allows insurance buyers to use third-party capital to fund their premium payments. Subject to the premium finance transaction, a premium finance company pays insurance premium on behalf of the policyholder, with the underlying policy serving as collateral for the loan. This allows the insurer to collect premium upfront and extend coverage to the policyholder without the need to tie up valuable assets or encumber any credit facilities. For insurance buyers of virtually any line of coverage, premium finance can serve as an effective cash management tool whereby the policyholder can both secure necessary coverage and preserve capital that can be used to meet immediate or long-term needs.

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Lending and Returning Profits to Captive Parents

Among other benefits, captives can extend loans to parent organizations or invest in other parent company assets, including real estate and trade receivables. A captive can also return profits to a parent via dividends and fund a parent's risk management expenses, including large risk consulting projects.

Whether a parent organization can pursue these strategies, however, depends on the financial health of a captive — namely, whether it can generate surplus and/or reduce the amount of surplus required by its regulator. Captive owners may be able to achieve this via:

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