

INSURANCE COST OPTIMIZATION STRATEGIES FOR PRIVATE EQUITY

Jeff Sharer

Vice President of User and Product Experience

LineSlip Solutions





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OVERVIEW

In a challenging landscape of economic uncertainty, high inflation, geopolitical headwinds, and more than \$530 billion in portfolio company debt and nearly \$1.5 trillion in commercial real estate debt coming to maturity in 2025, private equity funds and their portfolio companies are under continual pressure to reduce costs to maintain EBITDA levels amidst falling price multiples and higher financing costs.

At the same time, insurance costs continue to rise in many areas of insurance, with notable increases in real estate, energy, and transportation. To successfully navigate these hurdles and maintain profitability, risk management professionals in private equity must identify and execute a suitable insurance cost optimization strategy (ICOS).

ICOS can be a game changer. When leveraged effectively, the strategy allows firms to streamline and restructure to reduce costs, empowering professionals to strike the right balance between risks and insurance costs.


COMPREHENSIVE BENEFITS OF INSURANCE COST OPTIMIZATION

Insurance may provide a salve for the financial burden that may result from risk-related losses, but it often leaves one with a burn. When the loss comes, insurance may not provide the salve to cool the burn.

Many business leaders tactically manage insurance costs without seizing the more comprehensive opportunity to build strength into insurance cost structures and risk frameworks. Business management and information systems are typically designed for control – for instance, to deliver a budget – and are less geared toward providing transparency on insurance costs and their improvement potential. As a result, businesses making tactical top-down insurance cost restructuring decisions risk eliminating controls and resources that may be critical for future growth.

The increased operational leverage delivers short-term profitability when effectively identifying and executing the right ICOS. This lays the foundation for companies to overcome adversity and maintain a competitive advantage over the long run.

SETTING THE RIGHT APPROACH TO AN EFFECTIVE STRATEGY



There are three questions businesses need to ask to deliver ICOS successfully:

ONE

Is there a true understanding of the business' risk and insurance cost drivers?

TWO

What could or should the risk and insurance cost be to finance the firm effectively? And is this sustainable?

THREE

Does the business demonstrate the right competencies and mindset to deliver genuine cost savings rapidly?

Depending on their answers, executives can proceed with ICOS development using an approach tailored to their precise needs.

NEXT STEPS



After determining their business's ideal ICOS's scope, intensity, and timing, risk managers and business leaders take one of the following approaches:

Incremental Approach

Many businesses employ what can be referred to as an incremental approach. This is designed to offset pressures in a low inflation environment while delivering a few percentage points of cost optimization, at best. The usual starting point ranges from streamlining the number of insurance vendors (such as brokers) to reducing risk mitigation education spending.

Benchmarking Approach

A more tactical, top-down approach compares one's insurance and risk spending to its peers to identify cost-takeout opportunities. While this may achieve 5-10% of incremental savings, the risk is that benchmarking acts as a band-aid and fails to exploit the greater efficiencies that can be fully extracted from the insurance and risk cost. Implementing these risk mitigation activities may be require a broader buy-in that can be a challenge for some organizations.

Consultant Approach

This approach is business-driven, focusing on critical value drivers, scrutinizing all operations from the bottom up, and revealing the risk and insurance costs that significantly impact profitability. This approach often leads to better internal acceptance, given the collaboration required throughout the process. A consultant approach can improve margins by more than 15%; however, the cost savings produced may be substantially reduced by the consultant's implementation cost and often result in short-term gains, where costs may creep back in 12 to 18 months.



IDENTIFYING THE COST BASE

Private equity-owned firms and corporates evaluating their insurance and risk costs increasingly want to know the total cost for those assets. What benefit level could be achieved if all realizable cost-saving opportunities were realized?

Utilizing the LineSlip Solutions platform, one can quickly carry out a rapid value creation diagnostic to set the framework for considering insurance and risk costs concerning other levers at one's disposal. A diagnostic will drive unbiased cost transparency and lay the foundation of a delivery plan for short-, medium-, and long-term value creation. It will also inform crucial business decisions on whether to focus on fixing underperforming assets, pursuing sale options, or partially winding down an operation.

FOUR CRITICAL AREAS FOR VALUE CREATION THROUGH RISK AND INSURANCE COST REDUCTION

Once the ICOS approach and its scope have been determined, the next question is which insurance cost and risk areas should be targeted for improvement. Here are four key areas that risk management teams should address:

1. GET A GRIP ON SPENDING

Consider and examine all forms of risk and insurance spending, not only the premium, input, and vendor costs but elements of indirect expenditure as well.

- Employing traditional insurance procurement measures (e.g., consolidating demand, rationalizing, and developing closer cooperation with insurers and vendors) or evaluating alternative hedging mechanisms will likely deliver cost avoidance benefits instead of cost optimization, especially in a high inflationary environment. The key here is to ensure that the premium and risk are assumed to align with the weighted average cost of capital.
- To drive further cost optimization, entities must focus on reducing internal risks. This can be addressed by working with HR, Legal, Compliance, and Operations to harmonize services or deploy risk engineering to remove high-risk activities that don't deliver value.
- Similarly, scrutinizing insurance spending can prove highly effective: deciding which controls and policies should be implemented to reduce the internal need for third-party vendor spend (e.g., applying a zero-base lens)

FOUR CRITICAL AREAS FOR INSURANCE COST AND RISK REDUCTION AND VALUE CREATION

and driving sufficient value is essential. These steps often require an abandonment of the "how it's always been done" mentality, and an external, disruptive challenge is often necessary – one that is typically easier to initiate in a high inflationary environment.

2. SIMPLIFY WHERE YOU CAN

Business simplification enables sustainable cost optimization. Complexity grows in businesses over time, reducing productivity and increasing costs. This complexity makes it more challenging to fully grasp the businesses' true cost drivers.

Some key factors to consider are:

- Build an efficient operating model that can scale effectively, embracing productivity and back-office automation.
- Complexity is derived over time from organic growth, historical choices that may no longer be optimal under the current economic or regulatory environment, or acquisitions that weren't fully integrated. This can lead to duplication of roles, legacy systems, and infrastructure that often tie up resources and increases costs. Focusing on operating model optimization allows for increased agility, which is critical in navigating a high inflationary environment.

FOUR CRITICAL AREAS FOR INSURANCE COST AND RISK REDUCTION AND VALUE CREATION

3. FOCUS ON TALENT

Labor costs are critical to any ICOS. To offset inflationary wage increases, focus on productivity and remove activities with low-value add or duplication.

Recruitment teams today face an ongoing battle for talent, where skilled employees are increasingly expensive to attract and retain, with rising hiring costs forcing the broader use of contractors. The retention and development of talent, combined with recruiting exemplary high-quality leadership, are core factors in creating a value-driven culture.

4. THINK LONG-TERM AND HOLISTICALLY

Today's business leaders face unprecedented burdens, inflationary pressures, and talent shortages. To survive and thrive in this environment, businesses need to rethink their approaches to insurance cost reduction.

While traditional focus areas and methods are valuable, they often can't be performed due to inadequate systems and resources and usually only provide short-term gains, where costs may creep back in 12 to 18 months.

FOUR CRITICAL AREAS FOR INSURANCE COST AND RISK REDUCTION AND VALUE CREATION

Leaders must look holistically at their risks and insurance costs, bringing together a mix of competencies across commercial, finance, legal, operations, technology, and data analytics to focus on the immediate priorities that deliver sustainable value. If you cannot look at these matters holistically, reach out to LineSlip Solutions to start you on the path to sustainable value.





HOW LINESLIP CAN PROVIDE VALUE FOR PRIVATE EQUITY

LineSlip provides private equity firms with unparalleled insurance intelligence that revolutionizes and streamlines how they manage their insurance-related data. Our solution gives private equity a comprehensive view of their insurance programs across the entire portfolio. This comprehensive view ensures that private equity firms can stay in control and have a holistic understanding of their insurance program.

Our advanced analytics provides private equity with actionable insights to help them mitigate risks effectively, optimize insurance coverage across their portfolio, and make informed investment decisions.

LineSlip empowers those in the private equity space to drive better renewal outcomes, automate compliance reporting, and strengthen insurance governance. We help private equity firms strike the right balance between risks and insurance costs to maintain resilience and promote future growth.

To learn more about how LineSlip can provide value to private equity, [schedule a call](#) with one of our experts.



LINESLIPSOLUTIONS.COM



SALES@LINESLIPSOLUTIONS.COM



LINKEDIN.COM/COMPANY/LINESLIP-SOLUTIONS-INC.

ABOUT THE AUTHOR



JEFF SHARER

Jeff Sharer is LineSlip Solution's Vice President of User and Product Experience. He has more than 20 years of insurance experience as an underwriter, broker, and risk manager. Jeff has a proven history of managing all aspects of risk management and providing best-in-class cyber security, insurance, and operational risk management services. In his career, Jeff has held multiple executive leadership roles in various high-profile companies, including Goldman Sachs. As the industry has digitized, Jeff has focused his work on transforming risk information management to make better risk decisions.