



Cincinnati Fountain Square



# The CEO Resource

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## Insurance Costs Breaking Your Bank?- *Hard Insurance Market Dictates a Risk Management Review*

*The CEO Resource* is a periodic hot sheet of resource information for our colleagues, Chief Executives and Senior Management in business and leadership.

Our focus is to help senior management and company owners accelerate their pathways, first to "success" and then to "making a difference"- a significant difference for their families, their stakeholders and their communities. *The CEO Resource* is a time sensitive tool directly responsive to this critical focus.

### KMK Clients in the News

**Empower MediaMarketing** and the Health Alliance launched a new program to provide Tri-State residents with health information on the Web and on television. ([www.empowermm.com](http://www.empowermm.com))

**Vestar Inc.** received the Ohio Governor's Award for Excellence in Energy Efficiency for its program at the Cincinnati Metropolitan Housing Authority which resulted in annual energy savings of over \$875,000. They won the award last year for their program at Ohio University which is projected to create \$2.5 million in annual energy savings.

**dbaDIRECT** signed a contract to provide remote database administration services to Cincinnati Children's Hospital Medical Center. The Medical Center will use the Controller product, which offers database monitoring, maintenance, performance tuning, backup, recovery and reporting services.

**Downtown Cincinnati, Inc.** hired David Ginsberg as its new President/CEO. ([www.downtowncincinnati.com](http://www.downtowncincinnati.com))

Just over two years ago a client asked me – jokingly – whether I thought he should switch property and casualty insurance carriers in order to save \$100,000. He had stayed with his current carrier out of a sense of loyalty, even though the carrier did not have much expertise with his industry. This lack of expertise was highlighted when a minor claim was mishandled and threatened to exceed the policy limits.

My client was very surprised when I asked him a series of questions about his situation rather than immediately agreeing with him. Who was the new carrier? Who was the agent? Are they proposing the same coverages? Did they have a program designed for his industry? What is their AM Best rating?

The claim situation mentioned above had poisoned the relationship with the incumbent

carrier and had caused a significant rate increase. With these facts in hand, and having confirmed the answers to my questions, I told my client that he should feel free to change carriers, but that he should be prepared to see double, and maybe triple, digit increases in the next couple of years. I explained that the premium was so low because the company offering the coverage was from New York, and was buying their way into our region.

Sure enough, the next renewal jumped by about 50%. The next renewal was an increase of more than 100% accompanied by a decrease in coverages. Now my client was anxious and angry. "How can the rate jump like this when I haven't had any claims? Should I self-insure? Should I call the Insurance Commissioner?" he kept asking.

Welcome to the first "hard

market" in property and casualty insurance in over a decade.

By now, everyone has either heard that expression or felt the pain of the hard market themselves. Just what does this expression mean?

Traditionally, insurance has been a predictably cyclical industry. In order to attract more business, companies would lower their rates or expand coverages. However, as losses continued to occur, the company's loss ratios climbed over an acceptable level and the company had to raise rates. This cycle occurred throughout the industry and was made more or less acute by the market. If carriers could earn good returns on their money, the "hardening" of the stock market would be less acute. If not, you would see insurance environments much like the one we are in now.

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## Cashing Out: *The most important business deal of a business owner's life*

Today, more than half of all Americans (and nearly all of the readers of this article) own stock in publicly traded companies. The large, efficient stock markets make buying and selling ownership rights in companies very easy – all one has to do is call a broker or jump online to make a trade. The stock market, despite its recent shortcomings, has historically been a good vehicle for saving for retirement. When the time comes for retirement, investors sell their shares and use the cash proceeds to fund the activities and basic needs of the rest of their lives. Smart investors have diversified

portfolios of stocks, and thus the price attained during the sale of any single stock is not necessarily a make-or-break situation as far as the retiree's welfare is concerned.

The owner of a privately held company faces drastically different circumstances as he or she approaches retirement. Though a private company owner is likely to also own shares of publicly traded stocks, the owner's investment portfolio is usually less diversified than the retirees mentioned above. With rare exception, the business is the largest and most significant asset in the owner's investment

portfolio. For some, the proceeds generated from the sale of their company may serve as more than 90% of their personal wealth. Thus, the value attained from a sales transaction is paramount – the very livelihood of the owner and his or her family is directly impacted by the owner's ability to maximize the value of the sales price. Selling his or her company is the most important business deal in the career of a business owner.

Selling a privately-held business is far more challenging than selling shares in a publicly traded company. A large market of

(cont. on p.3)



## Site Selection- Valuable recon for your market growth strategies

Activity in the site selection industry has been slow over the last year or so due to a number of issues, including a slow economy, corporate scandal and shareholder fiscal watch-dogging, the continued threat of terrorist attack, and a potential war with Iraq.

A recent survey by *Area Development Magazine* gives us a valuable glimpse at what corporate executives across the country view as the most important factors when determining their location/expansion strategies.

### Survey results

The adjacent chart is a summary of the responses from the *Area Development's* readership. The majority of the respondents (75%) are involved in manufacturing while the remaining companies are involved in warehousing/distribution, software development, retail, financial services, and professional services. Forty-four percent have between 100 and 499 employees, 16% have 500-999 employees, and 34% have 1,000 or more employees.

During the last year, 56% of the respondents did not change their number of facilities, 15% added one or two, 14% added three or more, 8% eliminated one or two and 7% eliminated three or more facilities.

### Corporate Sentiment: We need to do everything we can to cut costs

The current recession has been hard on all industries, but the manufacturing industry has arguably been hit more than any other. Since companies have less control of their revenues, they have been forced to search for ways to control, and when possible cut, costs. They will ultimately find themselves in deeper financial problems if they continue to operate their businesses as they had during the mid-90s. Regardless of the industry, common targets of cost containment range anywhere from database administration to packaging to energy to insurance coverage costs.

What we can see from the responses to *Area Development's* survey is that cost containment is a major factor in the site selection process. Nine of the top ten factors listed are related to a manageable, or even controllable, cost. While tax exemptions and state and local incentives are listed separately, there are programs available to offset the costs associated with some of the other factors listed, including but not limited to labor costs, highway accessibility, environmental regulations, and occupancy or construction costs.

Just as businesses are experiencing hard times financially, so too are governments. State and local governments must attract or retain businesses to create positive economic impact. State and local incentives have had an enormous impact upon the site selection process because they assist the company in paying for its development without having a negative impact on its bottom line. These programs are available but require a sophisticated negotiation strategy.

It is no coincidence that most states have programs that address each of the top ten site selection factors. The programs are in place precisely to assist in lowering the cost of those factors most important to site selection decision makers. Companies considering any sort of growth strategy need to remember that these programs are available and that they require the proper due diligence and negotiation strategies.

When members of our team were with the Ohio Department of Development, they were intimately involved in crafting many of the programs related to relocations/expansions. Now on the other side of the negotiation table, they have experience assisting businesses in locating the best available programs and negotiating the deals. The importance of being able to decipher between policy and statute cannot be underestimated because it can have significant financial ramifications. Failing to put together the right team of experts to assist in formulating and implementing a growth strategy can be the difference between thousands and millions of dollars. Do you want to be the one in charge when your employees and shareholders realize that their pockets are affected by leaving money on the negotiation table?

To learn more, contact Jim McGraw or Joe Robertson at 513-579-6932. ■

COMBINED RATINGS* OF 2002 FACTORS			
SITE SELECTION FACTORS		2002	2001
<b>RANKING</b>			
1	Availability of skilled labor	90.9	91.6
2	Labor costs	89.9	91.5
3	Tax exemptions	88.2	82.7
4	State and local incentives	88.0	81.4
5	Highway accessibility	86.6	87.9
6	Corporate tax rate	84.6	79.0
7	Proximity to major markets	83.7	80.2
8	Occupancy or construction costs	82.4	82.3
9	Energy availability and costs	80.9	86.4
10	Environmental regulations	76.7	78.8
11	Availability of telecommunications services	76.1	83.3
12	Availability of land	75.2	79.7
13	Cost of land	74.0	77.3
14	Low union profile	69.4	78.0
15	Availability of broadband telecom services	66.7	61.3
16	Proximity to suppliers	61.8	67.1
17	Availability of long-term financing	60.0	48.7
18	Right-to-work state	58.0	67.6
19	Raw materials availability	56.0	64.6
20	Availability of unskilled labor	55.1	59.5
21	Accessibility to major airport	54.0	55.4
22	Training programs	44.7	51.4
23	Proximity to technical university	33.4	34.6
24	Railroad service	22.6	27.8
25	Waterway or oceanport accessibility	19.3	18.8

\*All figures are percentages and are the total of "very important" and "important" ratings of the *Area Development Corporate Survey*  
 \*SOURCE: *Area Development Magazine 17th Annual Corporate Survey*

## Capacity & Cost Management- More opportunities to save with dbaDirect's Outsourcing Solution

KMK Consulting Company's Capacity & Cost Management teams are specially designed groups of expert practitioners who focus on helping clients achieve efficiency for every expense. With cost savings in mind, KMKC is constantly searching for new ways to reduce our clients' operating costs and increase their profitability.

We frequently come across third-party groups

and companies that fit exceptionally well with the purpose and focus of our Capacity & Cost Management teams. When possible, we strive to develop relationships with these "best of class" organizations.

dbaDirect is a selective outsourcing company that provides remote database administration services on a 24 hour a day, 365 days per year basis. dbaDirect's database operation center

performs all of the functions of a full-time DBA staff for companies running Oracle, Sybase, Informix, IBM UDB and Microsoft SQL Server database technologies and enables companies to better manage their business-critical systems with fewer people at a lower cost.

With dbaDirect, clients are able to maximize (cont. on p.4)



## Let Your Taxes Pay for Your Development

Since the early 1990's the use of government provided economic development incentives has become common. Large multi-national conglomerates as well as local manufacturing companies vie for everything from low interest loans to training grants to tax credits. It is not unheard of for millions of dollars to be spent to attract or retain a major employer. Unfortunately, most states and municipalities are facing severe budget crises and the result could be a reluctance (or inability) to expend general revenue funds on economic development deals. However, all is not lost. Ohio, like most states, has incentives available whose size and availability are determined by the amount of investment and/or number of jobs created.

Performance-based incentives came about in the mid 1990's to assist states in being more competitive in pursuing economic development deals. Simply stated, the size of the incentive package available to a private-sector investor is based upon how much money it invests in land, building, machinery or equipment and/or how many jobs it creates or retains. The change in focus to performance-based incentives allowed states to avoid huge up-front subsidies to entice development that might not occur and also put the onus on the company to actually "do the deal." If the company pursuing the incentive fails to make the requisite investment or does not create or retain jobs, it does not get the

incentive. On the flip side, if it complies with its commitments, the company will receive the incentives. In fact, if the investment or job creation exceed original projections, the financial incentives received by the company will probably be greater than initially calculated.

It is because performance-based incentives are dependent on private-sector activity and not government budget balances that make them so attractive at a time like this. Essentially, a company can still receive significant financial benefit without having to worry about the availability of state incentive programs.

The following is a list of some of the programs available in Ohio and Kentucky that are triggered by private sector investment or job creation/retention. These programs must be carefully addressed as they can add significant value to a company as it pursues a development project:

- *Ohio Tax Increment Financing (TIF) District*
- *Ohio Enterprise Zones (EZ)*
- *Ohio Joint Economic Development District (JEDD)*
- *Ohio Job Creation Tax Credit (JCTC)*
- *Ohio Job Retention Tax Credit (JRTC)*
- *Ohio Manufacturing Machinery & Equipment (M&E) Investment Tax Credit*
- *Ohio Warehouse Inventory Tax Exemption*

- *Ohio Research and Development Sales Tax Exemption*
- *Ohio Technology Investment Tax Credit*
- *Kentucky Tourism Development Act*
- *Kentucky Rural Economic Development Act (KREDA)*
- *Kentucky Industrial Development Act (KIDA)*
- *Kentucky Jobs Development Act (KJDA)*
- *Kentucky Tax Increment Financing*

If a company is considering making an investment in land, building, machinery or equipment; or create or retain jobs, it can still benefit from the tax revenues it generates from the project. Therefore, a state's financial condition should not necessarily keep a company from pursuing available incentives.

It is critical, however, that the company position itself in a way that is beneficial to all parties involved, including but not limited to the company, the governmental body and the community in which the project will occur. There are several delicate factors involved in properly packaging economic development incentives. Failing to account for each of the elements may result in leaving money on the table and even effect the completion of the project as originally designed.

To learn more, contact Chip Gerhardt or Jim Benedict at 513-579-6548. ■

## Cashing out (cont.)

buyers and sellers is not readily accessible, an agreed upon market value of the business is not present, and the time to close the transaction is usually months as opposed to minutes.

Business owners who undertake the task of selling their business without the assistance of a professional advisor risk leaving money on the table. This result is largely born out of the fact that most business owners have little or no experience in selling businesses. Owners who fail to engage a professional often sell short because they do not properly value their company, they become too emotionally involved, and they court too few buyers.

Many times, owners fail to take into account the total universe of prospective buyers. Instead, they sell their company to a competitor in town or to an employee. Doing so may prove costly. Because different buyers value companies for different reasons, the key is to locate the buyer that places the highest value on an owners business. This

buyer may be a competitor or employee, but may also be a company competing in a different market, a company from a different industry, a financial buyer, or a group from outside the United States.

One of our current engagements is the sale of a \$35 million revenue manufacturing company. Our search for viable purchasers covered strategic and financial buyers that were local, regional, national, and even international in scope. As a result, we made contact with potentials buyers from North America, Europe, and Asia, and we received bids from companies and investment groups headquartered in Cincinnati, New England, Germany, and France. The benefit to the owner is that he was able to obtain maximum value for his company.

Locating a buyer is just one piece of the puzzle. Other tasks in the complex process of selling a business include: obtain and monitor confidentiality agreements, develop a business offering memorandum, facilitate

purchaser visits to the company, management presentations, and data room reviews, and negotiating the terms of the agreement with the purchaser.

To learn more about the Business Transactions Group at KMK Consulting, contact Tom Hayes or Matt Staarmann at 513-639-3876. ■

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### Insurance Costs (cont.)

Today's extremely hard market is being driven by a number of factors.

First, the stock market went into free fall. This reduced insurer's investment returns which had been running at historic levels right along with the market. This covered both the cost of lower premiums and claims. At the same time, the general economy started to weaken, weakening the corporate debt market. With investment income down, premiums had to go up in order to compensate.

Next, the terrorist attacks of September 11<sup>th</sup> resulted in more than \$50 billion in loss payments (and the claim on the buildings themselves still hasn't been settled!). That much capital leaving the industry reduces insurer's capacity, thus driving up prices.

The nature of the September 11<sup>th</sup> loss – international terrorists using hijacked aircraft as bombs – caused carriers to exclude terrorism coverage entirely from nearly all policies. The concern over the possibility of additional attacks drastically changed the risk profile for commercial buildings in major cities. Some carriers considered major restrictions on commercial property in cities considered at risk of a future attack.

These events occurred as the industry

was coming to the end of one of the longest soft markets in its history. Due to the prolonged soft market, pricing was very low, and coverages in many areas had been expanding for years. These conditions made the correction appear even more extreme.

While it is impossible to predict with any certainty, many think the market will remain in a "hard" cycle for another 18 to 24 months.

As for my client, he finally managed to place his insurance with a new carrier. Unfortunately, the premium was a 212% increase over the prior year, and a number of coverages – some critical, some not – were either eliminated or reduced. The insurance renewal process was reviewed and modified by the full board and should put my client in a better position to react if his company has a challenging renewal next year.

KMKC's Risk and Insurance Services Team is currently working with a number of clients to provide comprehensive insurance and risk management reviews of both property and casualty and group health insurance benefits. Please contact Paul Jacobs at 513-579-6581 for a preliminary discussion of your insurance and risk management programs. ■

### Capacity & Cost Management (cont.)

the productivity of their IT departments by re-deploying existing personnel from tactical support roles to higher-return, strategic initiatives. The company offers space management, backup/recovery verification, database fragmentation, monitoring key resources, database warning analysis, statistical updates, database integrity checks, and trend analysis services.

The primary benefits to customers include cost savings, around-the-clock support, in-house staffing and recruiting efficiency, and enhanced employee satisfaction.

dbaDirect's client list is growing fast, and some of the most reputable companies in the area have signed contracts with the database management company. Clients include Cinergy, Children's Hospital, and Western-Southern Enterprises.

To learn more about dbaDirect and the Capacity & Cost Management Services at KMK Consulting, contact Jim McGraw at 513-579-6932. ■