A Special Reprint of RRG CEO OF THE MONTH from

The
Risk Retention Reporter

How an MGA Saved His Business – It's Called Entrepreneurship

Featuring Louis "Lou" Schillinger, President & CEO
U.S. Rail Insurance Company, A Risk Retention Group

The entrepreneurial spirit is alive and well. Where? In the Risk Retention Group sector of the insurance industry. Just ask Lou Schillinger, President of U.S. Rail Insurance Company, A Risk Retention Group. Schillinger built a Main Street insurance agency with one shortline railroad customer into a Managing General Agency (MGA) that insures some 75 of the 400 major shortline railroads in the U.S., or more than 20 percent of the market.

Early on, Schillinger and a partner saw that shortlines were stepchildren in an industry dominated by Class I railroads. Many shortlines are feeders that bring cargo to the mainline operators. He and his partner seized on the underserved shortline market to offer insurance tailored to the needs of these smaller companies.

Their initial insurance markets were Bermuda Rent-a-Captives. In the eighties, major commercial carriers wrote the business. Schillinger's agency, United Shortline Insurance Services, was on a roll. However, after a few years two insurers merged putting his business in jeopardy. Schillinger turned to a London broker who placed much of the business with Lloyd's syndicates. After 9/11, fronting companies pulled out and syndicate support fell dramatically. He had to make a decision about liability coverage prompting the first question we asked Schillinger.

RRR: Why did you form the RRG?

Schillinger: We made a tactical decision to drop liability and concentrate on the Inland Marine property business that we placed with various commercial markets. However, after two years, it became clear we needed to offer the complete package including liability. At a conference, I began to learn about how Risk Retention Groups were filling the need for liability coverage. My partner and I decided to explore creating an RRG for the shortline industry.

RRR: Where did you raise the capital to launch the RRG?

Schillinger: We knew the shortlines needed us. So, we pre-funded the RRG with $1.5 million of our own money. I didn't mortgage the house – couldn't get away with that on the home front – but some of the big toys like the boat went away.

RRR: How did you structure the new company?

Schillinger: Working with actuaries and accountants, we created a stock company, U.S. Rail Insurance Co., A Risk Retention Group, and assigned 15 percent of the premium to capital. Over three years, this will allow us to replace the capital we put in.

RRR: U.S. Rail's first policy was issued October 27, 2007. Some would say this was a tough time to start a company given last year's economic meltdown. How are you doing?

Schillinger: We wrote $1,813,451 gross premiums in the first full year with a loss and loss adjustment ratio of under 30 percent. We now have 22 percent of the market. Our goal over the next three years is between $8 and $10 million gross written premium.

Louis M. Schillinger
President & CEO

RRG: U.S. Rail Insurance Company, A Risk Retention Group

Organizational Structure: A stock company owned by policyholders

RRG Member/Insureds: Shortline Railroads

Education: B.A.-Financial Administration, Michigan State University; Certificate in Railway Management, 2009, Michigan State Univ.; Certified Insurance Counselor, Society of Insurance Counselors

Experience: 22 years as MGA for shortline railroads and 30 years as independent insurance agent

Proudest Achievement: Putting together the first shortline-owned Risk Retention Group and obtaining an A-rated fronting carrier admitted in 50 states to share the risk

Biggest Challenge: Adjusting the demands of regulators, stockholders, directors, and our fronting company partners to manage the RRG and related business

RRR: Sounds ambitious. What's your business plan?

Schillinger: As an RRG, we offer the shortlines something they've always wanted – control over their own destiny. We differentiate the product to make what's left of traditional liability markets irrelevant. They compete on price. We compete on benefits. With the collapse of AIG, we're looked upon as the only safe harbor out there.

RRR: We hear that U.S. Rail is about to announce a risk sharing arrangement with a fronting carrier. What are your plans?

Schillinger: The carrier is National Interstate Insurance Company, a specialist in transportation that's owned by Great American. They insure buses and trucking companies but don't insure any steel wheels, so this will round out their transportation portfolio. U.S. Rail and National Interstate will share the risk. Policies will be written on National Interstate paper, so the RRG will become the reinsurer.

RRR: What's the advantage to your RRG shareholders?

Schillinger: Some shortlines have interchange agreements with Class I carriers that won't accept RRGs. Some large agents demand A-rated paper. The fronting arrangement solves these problems. Our producers won't have to become Surplus Lines agents. Some Errors and Omissions policies prohibit doing business with RRGs, so agents won't have to worry about losing E&O coverage. The shortlines retain control through the RRG. National Interstate gains access to a new class of business. Also, important, the fronting arrangement allows us to write more business because the risk is shared.

RRR: Can National Interstate become a shareholder in the RRG?

Schillinger: No. As the fronting carrier, National Interstate is a contract participant – not a shareholder.

RRR: Would you recommend that other startup RRGs seek fronting arrangements with an admitted carrier?

Schillinger: Yes. Or should I say, "yes – but." You need to have a relationship of trust and be sure the fronting carrier provides tangible benefits. A great deal of due diligence is required. Don't expect to find a fronting carrier unless your RRG has a strong capital base.

RRR: How do you juggle running the MGA, working with traditional carriers on the property side, and growing the RRG into a significant player on the liability side?

Schillinger: I wear two hats. On the MGA side, I'm commission driven. On the RRG side, I'm profit driven. I like managing multiple enterprises at the same time. I have a strong underwriting team that keeps me grounded. I won't put risks on the books with big potential losses. As a business man I welcome the challenge of finding solutions to difficult problems.

Louis M. Schillinger
A Case Study in Entrepreneurship

Lou Schillinger's experience provides a case study in entrepreneurship. He built a successful business as an MGA insuring shortline railroads. He tapped a variety of markets from Lloyd's syndicates to domestic insurers to offshore captives. When the liability insurance markets dried up, he tried to retain the property business, but soon learned the customers wanted a complete package. So, he put up his own money to launch the RRG. After a couple of years, he found a fronting company to share the risk and kick start growth. Schillinger went from "dialing for dollars" as a Main Street retail agent to building a complex business structure to serve an important niche market. That's entrepreneurship.

RRR: How does your role as a Managing General Agency help retail agents who write shortlines? Is forming an RRG something MGAs in other businesses should look into?

Schillinger: We do business through some 85 agents. Eighty of them have only one shortline customer. These retail agents have very limited knowledge of the railroad business. We've been writing property and liability coverage for shortline railroads for 22 years, so we know their needs and can work directly with them to design coverage and provide professional risk management. Our agents welcome this support. A managing general agency that has difficulty finding and retaining markets to insure the liability risks of its customers may well find that forming an RRG is the answer. It worked for us.

RRR: What lessons have you learned in the last couple of years that would help startup RRGs in other industries?

Schillinger: Getting an RRG off the ground is neither as rosy nor as disastrous as people may tell you. It will take more time than you expect, and in the beginning the revenues may fall short of expectations, so be flexible. Don't get married to your preliminary business plan. Be prepared to adjust your tactics, but stick to the basic strategy of providing stable, affordable liability insurance.

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