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Captives need a FERMA footing

The Federation of European Risk Management Associations (FERMA) has launched a campaign to change tax authorities and other public bodies' misperceptions about captive insurance.

To kick off the campaign, FERMA has released a position paper on captive insurance companies and the advantages they have for the European economy.

The position paper will also be submitted to the Organisation for Economic Co-operation and Development so that the views of European risk managers are considered when discussing the implementation of base erosion and profit sharing (BEPS).

The position paper stated: "FERMA believes it is crucial that tax authorities understand the positive technical risk management aspects that captives can represent for multinational organisations."

"Although FERMA is convinced that EU domiciled captives will pass the BEPS test, the administrative costs of owning a captive are very likely to rise."

"As a consequence, there will be an increase in the total costs of doing business that will not help accelerate economic growth."

FERMA has also asked its 22 member associations across Europe to share the position paper with national tax authorities to explain the real value of captives, as they will be responsible for deciding the implementation of BEPS measures.

The paper will also be brought to the attention of the European Commission and Parliament, and the European Insurance and Occupational Pensions Authority stakeholder group, to increase their understanding of the role captives play in the European economy.

It is intended to help inform the group on how a captive can help improve European businesses and some of the advantages captives have, such as being Solvency II regulated.

Jo Willaert, president of FERMA, commented: "We find it ironic that Solvency II was designed to include, as much as possible, captives as normal regulated insurance companies, despite requests from the risk management community for more proportional regulation, and now BEPS and commission initiatives are differentiating captives from the rest of insurance companies."

Turn to page 22 to find out more.

Greek businesses to tackle cyber crime problems

Greek businesses are increasingly looking to insure themselves against cyber attacks such as data breaches and ransom attacks, a new report has found.

Timetric's report, Reinsurance in Greece, Key Trends and Opportunities to 2019, provides a detailed analysis of the market trends, drivers and challenges in the Greek reinsurance segment.

It found that most cyber attacks in Greece are unreported, as companies are either "unaware of attacks or just ignore them".

The report stated: "The government is making an effort to increase the awareness of cyber risk insurance through the 'Cyber Crime Unit'. This will help businesses and organisations to understand and identify and mitigate cyber-risks, and tackle incidents such as cyber-attacks or data breaches."

Canada is key for Cayman captives

Canada is a key market for Cayman Islands captives, according to Kieran O'Mahony, chair of the Insurance Managers Association of Cayman (IMAC).

The Cayman Islands captive insurance industry continues to build its position within the Canadian market, according to IMAC.

Industry professionals from the Cayman Islands attended the 2016 Risk and Insurance Management Society (RIMS) conference, held in Calgary between 11 and 14 September, where they discussed the benefits of doing business in Cayman.

O'Mahony said: "With the 2011 tax information exchange agreement between the two countries, the strength of our legislative and regulatory infrastructure, and the extensive experience and expertise of our local service providers, Cayman offers Canadian companies a product that is well-tested and efficient."

He added: "Our business cultures are similar and our laws are common-law based, and with a number of Canadian captives already domiciled in Cayman we are excited to have this opportunity to continue the trend and to explore these synergies further."

R&Q looking ahead to new deals

Randall & Quilter (R&Q) Investment Holdings will complete various insurance company transactions in the next few months, according to the group's latest results.

Contents

Captive Insight
The captive industry needs to come together to respond to the challenges and threats that it faces
page 8

Domicile Profile
The Isle of Man is busy making key regulatory changes in the insurance industry
page 12

China Insight
China is looking to strengthen the boundaries of captive insurance strategies
page 14

Captive Collateralisation
An understanding of collateralisation is becoming increasingly important
page 16

Cyber Risk
It will be interesting to see how regulators begin to craft legislation around cyber risks
page 20

FERMA Perspective
FERMA's new position paper challenges the misperceptions of captive insurers
page 22

ILS Update
Exchange Re recently became the first ILS-based cell structure in Malta
page 24

Domicile Outlook
Malta can and is fully utilising its potential in the insurance industry
page 26

Catastrophe Risk
The Cook Islands has enacted the Pacific Catastrophe Risk Insurance Facility Act
page 28

Claims Management
Captive and risk managers need to be in control of their claims processes and information flow
page 30

DIMA Update
There is a lot still in store for the Dublin International Insurance & Management Association and its members
page 32

Industry Appointments
Comings and goings at JLT, Allianz X and the National Association of Insurance Commisioners
page 34

The transactions range from UK insurance company acquisitions to US novations, loss portfolio transfers and the purchase of onshore and offshore US and UK captives, with “a notable trend towards larger transaction sizes and reserve balances”.

The report found that net reserve releases from run-off insurance companies totalled £6.2 million, higher than the previous year, when they stood at £4.3 million.

According to the report, this was led by the proactive claims management strategy in R&Q Re, previously impacted by the ACE surplus maintenance agreement, which was reduced at the end of last year.

The report stated: “La Licorne, R&Q Alpha (previously IC Insurance) and our Guernsey captive consolidator, Capstan, were all additional contributors to the positive reserve development in the period through a combination of favourable settlements and interim reserve reassessments.”

The results also showed that R&Q’s pre-tax profit for H1 2016 was £1.2 million, compared to a loss of £4.5 million for the same period last year.

R&Q’s gross written premiums stood at £21 million in H1 2016, compared to £13.5 million in H1 2015.

Ken Randall, chair and CEO of R&Q, said: “I am pleased to report that the group delivered a significantly stronger performance during the first half of the year compared with 2015, especially when factoring in the additional £5 million boost from foreign exchange gains, not taken through the group’s pre-tax profit. The group’s result is always heavily second half weighted and this year is no exception.”

He added: “The ever increasing supply of new capital to the insurance industry and the expansion of alternative risk transfer vehicles continues to challenge the pace of delivery of attractive income growth and profits in our live operations.”

Insurance Europe ‘concerned’ over BEPS proposal

Insurance Europe has expressed concern over certain proposals relating to base erosion and profit sharing (BEPS) and their potential impact on the insurance sector.

The Organisation for Economic Cooperation and Development’s (OECD) final proposals for the BEPS project, which aims to harmonise global tax rules on profit shifting, require “additional guidance on how the rules would apply in particular for permanent establishments (PEs) outside of the financial sector”.

“For some insurance business models, PEs would be recognised for tax but not for regulatory purposes with nil or minimal additional profit being attributed to them,” Insurance Europe explained.

In a statement, Insurance Europe said: “This would represent a disproportionate compliance burden for insurers, as well as for tax authorities.”

“While the discussion draft recognises that there will be situations in which the profits attributed to the PE will be nil, it fails to propose a solution which would avoid the disproportionate compliance burden that will be created for insurers in these cases”.

Insurance Europe said the final proposals are “disappointing” and that it disagrees with the suggestion that “PEs may nevertheless be justified by the potential existence of ‘other tax liabilities’”.

The deadline for comments on Action 7 of the BEPS Action Plan report was 5 September.

The OECD intends to hold a public consultation on current BEPS discussion drafts on 11 and 12 October at the OECD Conference Centre in Paris, France.

China Re keeps ‘A+’ rating

The net profit of China Reinsurance Corporation (China Re Group) declined by 59 percent during the first half of 2016 due to a significant drop in net realised investment gains.

However, according to S&P Global Ratings, the ratings on China Re Group and its subsidiaries, China Property & Casualty Reinsurance, and China Life Reinsurance, will remain unaffected by the decline in net profit.

S&P’s decision “considers the group’s capitalisation to remain supportive of its credit profile despite lower profit, which was largely due to a significant drop in net realised investment gains”.

S&P said: “We expect the persistent weakness in investment conditions to continue to put pressure on China Re Group’s operating performance in 2016. However, we anticipate that the combined ratio of the group’s property and casualty segment will remain stable during this time.”

The ratings company suggested that China Re Group will maintain its position in the domestic reinsurance market in China, “despite a likely gradual decline in the group’s domestic P&C reinsurance premium income in 2016 and 2017 due to higher retention of risks by direct P&C insurers in China”.

USA Risk becomes WBN member

USA Risk Group has been approved as a member of the Worldwide Brokers Network (WBN).

USA Risk is headquartered in Vermont but has additional offices located in captive domiciles such as Bermuda, the British Virgin Islands, Arizona, Barbados, the Cayman Islands and South Carolina.

Francie Starnes, CEO of WBN commented: “We are delighted that USA Risk has chosen to join our portfolio of high quality firms offering essential insurance- or benefits-related services for WBN member firms and their clients.”

Paul Macey, head of captive management for USA Risk Group, added: “USA Risk Group is proud of our independence and we are delighted to be approved as a member of the WBN.”

Marsh acquires employee benefits group

Marsh & McLennan Agency (MMA) has acquired Benefits Advisory Group, an Atlanta-based employee benefits consulting firm.

Benefits Advisory Group provides employee benefit services to midsize employers in Georgia.

All of the firm’s employees, including its owner Al NeSmith, will join MMA, and will operate as part of MMA’s existing Atlanta operations. Terms of the transaction were not disclosed.

Thomas Brown, vice chairman of MMA’s Mid-Atlantic region, commented: “We are pleased to have Al NeSmith and his team join the Mid-Atlantic region of MMA.”

Istmo Re ratings downgraded

A.M. Best has downgraded the financial strength rating to “B++ (Good)” and the issuer credit ratings to “bbb” of Istmo Compañía de Reaseguros (Istmo Re), Aseguradora del Istmo (ADISAP) and Liffey Reinsurance Company (Liffey Re).

Istmo Re and ADISAP are both located in Panama City, Panama, while Liffey Re is located in Dublin, Ireland.

According to A.M. Best, the downgrades reflect the companies’ “deterioration in financial flexibility derived from increasing

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financial leverage, limited growth prospects and a downward trend in operating performance, reaching negative levels at year-end 2015".

The ratings downgrade of ADISAP and Liffey Re are the same actions as those taken on their parent company, Istmo Re.

A.M. Best said: "The rating downgrades and the under review with negative implications status of Liffey Re reflect the full dependence of the company on Istmo Re's business as its captive retrocessionaire and deterioration in operating performance."

"Liffey Re's ratings will move in tandem with those taken on Istmo Re."

Atlas Insurance secures South Carolina captive licence

Atlas Insurance Management has secured approval from the South Carolina Department of Insurance to act as an insurance manager for the captive business in the state.

Atlas is the first North Carolina-based captive manager to be approved by the South Carolina Department of Insurance.

Martin Eveleigh, chairman of Atlas Insurance Management, said: "We are truly pleased to have obtained approval to act as a captive manager in South Carolina."

"The addition of South Carolina to our portfolio will expand the captive options available to our clients, and we look forward to working with such an established, well-respected domicile."

AUSTRAC improves cyber protection

AUSTRAC, Australia's primary financial intelligence agency, has established a new cyber team to identify and combat cyber crime, including online terrorism financing, money laundering and financial fraud.

The new team will use financial and cyber intelligence to investigate online payment platforms and financial cyber crime to protect against money-laundering and criminal networks.

Michael Keenan, minister for justice of Australia, said: "We know that the use of fraudulent identities continues to be a key enabler of serious and organised crime and terrorism."

Kennan revealed that the agency will also work with iDcare, Australia and New Zealand's national identity support service, "to target job recruitment scams that organised criminal syndicates use to recruit innocent people as money mules".

The team will also work with the Australian Cybercrime Online Reporting Network and Joint Management Group to identify patterns and trends that could lead to large-scale financial scams, according to Kennan.

The AUSTRAC cyber initiative forms part of the Australian government's Cyber Security Strategy, announced by the Prime Minister in April.

Kennan added: "Our agencies are leaders in their interconnectivity and intelligence sharing, and this cyber team will further boost these efforts."

"Strong cyber security underpins Australia's economy and is a major priority for the Australian government."

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The end of the beginning

It's time the industry came together to form an effective, united and coordinated response to the many challenges and threats it faces, says Malcolm Cutts-Watson

"Once more unto the breach, dear friends, once more … when the blast of war blows in our ears, then imitate the action of the tiger; stiffen the sinews, conjure up the blood, disguise fair nature with hard favoured rage."

Shakespeare's famous lines are a rallying call by Henry V to his English troops to defeat his French enemy. It seems to me that now is the perfect time to raise a similar rallying call to the captive industry globally to get its act together and form an effective, united and coordinated response to the many challenges and threats it faces. I do not have the space to list the various fiscal, political and regulatory initiatives underway globally and I suspect readers will have little appetite to trawl through another inventory of threats. But I am not alone in recommending such a course of action—captive practitioners and media partners are also making similar pleas.

So why am I making this call to arms and why hasn't the industry already coalesced into a unified front? To date, threats to captives have been addressed at a domicile level or by forming ad hoc alliances when the threat has been regional and/or common to several domiciles. This tactic is unlikely to remain effective as threats become global and their source supranational.

So are there any candidates to assume this global coordinating role from among existing captive associations? I've researched the history of the various bodies representing the captive industry across many domiciles and regions and they seem to follow a similar growth pattern. The zoologist in me naturally looks for analogies in the animal kingdom and I cannot but cite the theory of convergent evolution. This is the independent evolution of similar traits, where several species respond to similar challenges in a similar way. An obvious example is flight, which has evolved in birds, insects and bats, albeit with different wing structures.

Figure 1 below shows high similarities between the associations' key features. Although Vermont has been the most progressive with respect to membership and objectives, associations are, on the whole, inward looking and seek to protect that domicile's position. There is only passing reference to international development or liaison.

Figure 1 also suggests that, other than Vermont, the domicile associations' titles make reference to manager or management, which suggests an emphasis on the practical aspects rather than international vision. Finally, it shows that captive managers have significant directorial governance influence.

Figure 1: Captive associations assemble

Domicile	Vermont	Bermuda	Cayman	Guernsey
Captive association	Vermont Captive Insurance Association.	Bermuda Insurance Management Association. Offshoot, Bermuda Captive Owners Association.	Cayman Insurance Managers Association, then Insurance Managers Association of Cayman.	Guernsey Insurance Managers Association, then Guernsey Insurance Management Association, then Guernsey International Insurance Association.
Year founded	1985	1977	1993	1983
Objectives	Work in best interests of members, captive education, connectivity at events, lobby at state and federal level, maintain an environment favourable to continued growth.	Protect members and members clients' interests, liaise with government or any association or body on matters that concern members, encourage professionalism.	Promote the development of the local captive industry through engagement with local government, regulators, media, and other organisations, promote integrity and intellect of the industry, encourage sustainable growth.	Represent interests of members, promote insurance industry in Guernsey and internationally, forum for exchange of ideas.
Membership	Open to captive owners, captive managers and service providers.	Captive managers (and self-managed captives) and service providers.	Initially captive managers, then open to captive owners and service providers, according to sources.	Initially captive managers, then open to captives and service providers and finally to non-captive international insurers.
Governance	Captive owners form a minority of board of directors. Chair is a captive owner.	Executive committee members and chair are captive managers.	Executive committee members and chairman are captive managers.	Vast majority of executive committee and the chairman are captive managers. No captive owners represented.

My conclusion from Figure 1 is it is unlikely that any of the domicile associations will have the drive, mandate and strategic imperative to rise above parochial matters. This is not a criticism.

These organisations perform an excellent job representing their members' interests but lack the mandate to assume the needed broader international strategy setting and coordination role.

But aren't there organisations that represent captive owners and are domicile neutral? Of course, and Captive Insurance Companies Association (CICA) and European Captive Insurance and Reinsurance Owners Association (ECIROA) immediately come to mind. Both represent regions: CICA is predominantly US-centric and ECIROA, as the name indicates, is Europe-based.

My guess is, in due course, there will be an equivalent organisation in Asia as the captive industry in that region flourishes. Do any of these captive owner-led organisations have the appetite to take on a global unifying role?

There are some positive signs: both are free of jurisdictional or commercial ties since they are not linked with a domicile or government; both have a board of directors with a majority of captive owner representatives; CICA has a European representative on its board of directors and references its role as "an advocate around the world and a valuable connection to the captive industry"; and ECIROA talks of "a forum to exchange experiences across borders" (but I wonder if this relates to pan-European and what impact will Brexit have?), and runs, in association with CICA, a biennial conference in Luxembourg.

So some encouragement, although the last time I raised the issue of CICA assuming this global role, I was informed it has been looked at before and rejected, and that it would be too expensive. Having said that, I imagine CICA's agenda has been pretty full.

There is also a perception that ECIROA was formed on a single-issue mandate—Solvency II. Now that this is enacted, does the association have the motivation to take on a global coordination remit? ECIROA has recently issued papers on base erosion and profit shifting (BEPS) and captives, which suggests this may become its next project.

CICA is currently recruiting a new leader to replace the departing president, Dennis Harwick, and I see this as a great opportunity to put global strategy, coordination and promotion into the job description to attract someone who has the vision and the appetite for the challenge to bring the industry together under one global umbrella organisation. It would be a massive task, but what a legacy to leave.

Convincing the various captive stakeholders as to the value of such an enterprise, obtaining commitment and securing a budget will require special leadership, but it can be achieved. I imagine a number of multinational companies with a significant investment in, and commitment to, their captives would be willing to support, and make resources available to, such a venture.

Speaking to Harwick, he advises that CICA investigated such a role and had begun a recruitment process for an advocacy specialist, but the venture collapsed when captive owners and managers were asked to make an investment.

Their response was, in principle, support, but they showed a reluctance to put their heads above the parapet and fund, at that time, a non-specific item. Today's circumstances make those defences short sighted and inappropriate.

You may be thinking that couldn't the risk management community pick up this mantle? Risk management associations such as the Risk Management Society (RIMS), Federation of European Risk Management Associations (FERMA) and Association of Insurance and Risk Managers in Industry and Commerce (AIRMIC) obviously have an interest in captives but it is not, and never will be, their raison d'etre.

However, I suspect they would be supportive of any integrated global captive industry initiative. But this initiative will need to be driven by the captive industry itself.

To me, the best route to success is to look to a captive owners' association to step up and assume the role of global coordinator of the captive industry. Of the candidates, CICA appears to demonstrate the most potential and is going through a period of leadership change so this mandate could be included in the association's vision, governance and strategic planning.

It is up to CICA's membership to step up to the plate and support such an altruistic initiative, and other captive associations to agree to CICA taking the lead.

I do not see it as feasible to add an additional layer to the captive association hierarchy through the creation of a new global captive association. This would create duplication of effort and cost and I suspect would not be fully supported by the various captive communities worldwide.

Better to start with CICA, expand its objectives and establish a governance framework that would allow captive stakeholders worldwide to be able to contribute to, and be part of, the new organisation.

The committee system that already operates successfully could be expanded and further representatives from domicile associations invited to participate. In terms of governance and optics, I would suggest the board of directors continue to contain a majority of captive owner representatives.

These are just some initial thoughts of mine. I'm sure there are many others with better ideas and the ability to convert these into deliverables. The purpose of this article is to give the debate some momentum and to urge key stakeholders to engage. Delay could significantly adversely affect captive business in all domiciles worldwide.

As Sir Winston Churchill said: "Now this is not the end. It is not even the beginning of the end. But it is, perhaps, the end of the beginning." **CIT**

Malcolm Cutts-Watson
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Like a regulatory stone

The Isle of Man is pressing ahead with regulatory reforms

In a bid to further develop the Isle of Man as a domicile, regulators have made some key regulatory changes.

At the end of last year, the Isle of Man government decided to merge the Insurance and Pensions Authority (IPA) and the Financial Supervision Commission (FSC) together under a single regulator.

The integration between the existing IPA and FSC functions would be a long-term objective that would need to be approached with due consideration by members of the authority.

With the new combined regulatory authority system came a new chief executive, Karen Badgerow, who relocated from her previous role in Canada to the Isle of Man Financial Services Authority.

The Isle of Man has also seen other regulatory changes, including the material changes to accounting standards from 1 January this year, which altered the reporting requirements for captives and captive managers.

In addition, Ross Dennett, chairman of the Isle of Man Captive Association, reveals there are also plans to launch the first quantitative impact study (QIS) for the non-life insurance sector in the next few months.

Dennett explains: “Whilst such initiatives require participation, time and effort from the industry, they ultimately all add value and security to our clients.”

Currently, the Isle of Man has approximately 120 captives licensed in its non-life sector, and last year saw the island’s gross premiums written reach £1.4 billion and funds under management total around £6.3 billion.

Most of the captives domiciled in the Isle of Man are UK-parented organisations representing a range of industry sectors such as energy, engineering and manufacturing.

According to Badgerow, the Isle of Man is a “very mature” captive domicile and has experienced a quieter year in 2016 so far. She suggests that this is due to uncertainty around Solvency II at the start of 2016 and, of course, the Brexit vote.

Solvency II

Although the Isle of Man is not a member of the EU and therefore is not subject to the Solvency II regime, Badgerow notes that the Solvency II regime for some captives will result in additional costs from a capital, and compliance perspective.

She reveals that to date, the Isle of Man is yet to see an “influx of insurers seeking to redomicile from Europe to the Isle of Man as a direct result of the implementation of Solvency II”.

However, Dennett says, “the sector is certainly seeing several specific examples of clients with captives domiciled within the EU seeking a simpler and pragmatic approach”.

He says: “This is particularly the case with simple structure captives with relatively conservative risk retentions. Minimum capital requirements can certainly be excessive this being compounded by overly burdensome Solvency II compliance. Of course Solvency II is fundamentally good business practice, however, for a simple captive company can be way over the top.”

Badgerow reveals the island is currently updating its own regulatory framework in accordance with international standards and will be introducing its own risk-based capital regime.

OECD and BEPS

The insurance industry is also experiencing ongoing issues around tax matters in terms of the increase in the UK’s insurance premium tax and diverted profits tax plus base erosion and profit shifting (BEPS), which Badgerow claims “all potentially create a level of uncertainty”.

The BEPS Action Plan, released by the Organisation for Economic Cooperation and Development (OECD) and endorsed by the G20 countries, has "naturally drawn a lot of attention", according to Dennett.

The report on the 15 BEPS focus areas reflects recommendations for significant changes in international tax law and treaties. Dennett suggests the attention has now turned to the actions that are taken by countries in response to these recommendations.

He says: "Inevitably the introduction of the BEPS framework will have an impact across the board, therefore the Isle of Man is not unique or specifically any worse off than any other countries and/or domiciles. It is a level playing field."

While BEPS will be on the agenda for monitoring and review by many owners of captive insurance companies, captives are not established primarily as a means of reducing tax liabilities.

Badgerow suggests that BEPS will be one of a number of issues being considered by risk managers when considering their group's overall risk strategy.

Dennett reveals that the Isle of Man is yet to see any concern from captive owners over BEPS and notes that for captives managed responsibly, the tax-related advantages are secondary.

He says: "Most captives are professionally managed in accordance with strong corporate governance control and are therefore subject to robust protocols around premium benchmarking, claim and incurred but not reported reserving."

Brexit

After the UK's decision to leave the EU in June, there has been a lot of questions around what a Brexit will mean for the captive industry. Arguing although the Isle of Man is located outside of the EU, and not directly affected by the Brexit vote, Badgerow reveals that regulators did some work in advance of the vote to understand what the impact would be.

She notes: "Most of our firms in the captive and non-life markets are UK-parented and it will depend on the extent to which the decision to exit the EU impacts them."

There has been talk of whether Brexit could increase interest in domiciles such as the Isle of Man and other domiciles situated outside the UK, however, Badgerow claims: "Everyone seems to be taking a wait and see approach in terms of what the impact may be".

In the meantime, she explains that it is important for the Isle of Man to work on updating its regulatory framework around the International Association of Insurance Supervisors insurance core principles project and the development of a regulatory regime that will be considered equivalent to Solvency II.

Badgerow says: "That work will continue to be important regardless of the UK being in or out of the EU because for our firms who do want to work or conduct business locally it is really important that the Isle of Man completes its regulatory review."

She adds: "At the end of the day the proposition to have a captive is still very attractive for many firms." **CIT**

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Setting the foundations

China is looking to stretch the boundaries of captive insurance strategies, according to Dominic Wheatley of Guernsey Finance

There has been much comment recently about the development of insurance and risk financing in China, and particularly about the growing interest in the use of captive insurance companies among Chinese corporations.

Of course, the readership of this publication is aware that captives are well-established strategic tools among the world's top companies with the vast majority of them using captives for a variety of purposes and across the full range of corporate risks. However, to date, their use has been limited among major Chinese corporation.

The reasons for this are not difficult to see. As most assets and corporations have been publicly owned in China, risk has simply been assumed by the government and losses met out of current government revenues. Not surprisingly, insurance has not recognised as necessary by managers or their public sector shareholders. However, the move toward a more mixed economy, and a more international outlook, has seen two significant trends: the emergence of private sector corporations; and the increasing privatisation of government-owned companies.

These changes in ownership and governance, and the exposure to international management practices, have increased recognition of the economic efficiency of insurance in a general sense (personal lines insurance is also fast growing alongside the emergence of an affluent middle class in China), and the financial efficiency of formal risk management, risk transfer and risk financing models. As ever in China the rate of progress and adoption of sophisticated techniques is faster than outsiders expect and is set to accelerate over the coming years.

The first tentative steps to explore captives have involved non-Chinese assets and taken place in traditional captive centres. However, the attention is now switching to domestic risks and establishing a captive centre in mainland China. The assimilation of the technology involved is rapid and is matched by development in their chosen internal captive centre, Kashgar, in the Xinjiang region of Northwestern China, and the establishment of the China Captive Alliance (CCA) as the trade association for its fledgling captive insurance industry.

The inaugural Asia-Europe Captive Summit in Kashgar in June of this year marked important steps towards linking up the domestic captives with their overseas sister-captives writing international risks and coordinating and consolidating global insurance programmes. These included a technical support agreement between the CCA and the Guernsey International Insurance Association, and a captive promotional agreement between the Kashgar Trade Development Zone and Guernsey Finance.

All of this progress is being encouraged and facilitated by the China Insurance Regulatory Commission (CIRC) and China's other financial regulatory bodies, and is enthusiastically endorsed by the People's Bank of China. Discussions are already underway towards a memorandum of understanding between the CIRC and the Guernsey Financial Services Commission, which should enable operational and financial efficiencies and provide enhanced transparency and joined up regulatory oversight. This will bring the operational and strategic benefits of captives and holistic risk management to bear on Chinese corporations on a global basis.

These developing arrangements are a major step forward toward China's goal of developing its own domestic international insurance expertise and a mature insurance industry, as well as increasing its international insurance relationships. For Guernsey, they represent a significant broadening of Guernsey's growing business relationship with China, which stretched back to 2007 when we appointed our first Chinese representative, Wendy Weng, in Shanghai. Weng has been highly instrumental in encouraging the development of captive technology in China and broking the various relationships that are now helping shape China's captive future.

They also further enhance Guernsey's reputation as the leading centre for the management, governance and regulation of global captive insurance programmes.

What will this achieve?

In general terms, three benefits will accrue to China and Chinese corporations out of these developments.

Firstly, China will gain access to the substantial accumulated expertise and experience of Guernsey's long-established captive industry. This includes the intellectual property involved in administering captive insurance companies, as well as the innovation for which Guernsey is known, and its world-class captive regulatory environment. Also included are its knowledge

and experience of delivering programmes into diverse regulatory environments around the world, and the optimal use of captives for maximum strategic effect. Finally, China will benefit from Guernsey's network of counterparties in London, Zurich and elsewhere. Through working with Guernsey's industry, China will in time be able to assimilate this knowledge and network to the enhancement of its own captive industry.

Secondly, Chinese companies will be able to develop global programmes based around Guernsey captives utilising all of the accumulated experience and expertise of Guernsey's insurance industry, and with ready access to that of the London market as well as to its considerable reinsurance capacity. These arrangements will coordinate their programme delivery and consolidate their global risks, and could ultimately be onshored back into their domestic captives in Kashgar, providing significant capital efficiencies and streamlining their governance and reporting lines.

Thirdly, Chinese captive owners will be able to make use of their access to expertise in other classes as they look to extend their initial property programmes, including taking advantage of soft-market multi-line capacity in the London wholesale markets, employee benefits, casualty, and emerging risks, such as cyber.

Guernsey can also advise on non-conventional programme designs, risk transfer pricing, and detailed terms and conditions. Its robust governance, regulation and the considerable substance of its insurance community will ensure captive arrangements are respected by international regulatory and tax authorities, and work in harmony with the non-captive elements of insurance programmes.

For its part, Guernsey will benefit not only in terms of new captive business, but in terms of developing our understanding of Chinese business and corporations, their risk environment and attitudes to risk and risk financing, and the strengthening of our trading links with China.

Of course, multi-domicile captive strategies are not new but they did take decades to develop elsewhere. It is a measure of China's ability to adopt technology quickly that just a few years after establishing its first captives it is already looking to stretch the boundaries of captive strategies.

The future for captives in China is secure and is coming quicker than you may think. **CIT**

Dominic Wheatley
CEO
Guernsey Finance

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Credit where it's due

As more employers look to incorporate captives into their risk and benefits management strategies, an understanding of collateralisation will become increasingly important, according to Phillip Giles of QBE North America

The primary motivation for an insured to participate in a captive or other alternative risk programme is to control the ultimate cost of risk by reducing their reliance on traditional insurance coverage. As a result, the employer retains more predictable layers of risk while transferring more unpredictable or catastrophic layers to an insurer. The insured also maintains the ability to strategically deploy surplus and realise the potential profits generated through underwriting and investment returns. The amount of profitability return will be proportionate to the amount of risk retained by the insured and held within the captive arrangement.

One of the most important, and often misunderstood, components of a captive or other alternative risk programme is the amount of collateralisation required of the insured by a fronting carrier to secure the portion of risk retained within the programme. Within the overall structure of a fronted programme, the captive becomes a reinsurer of the issuing carrier. The carrier is agreeing to cede a portion of the risk, as reinsurance, to the captive, which is owned by the insured. Viewing the importance of collateralisation from a carrier's perspective will be helpful in providing more understanding to an insured.

Closing the credit gap

An insurance carrier faces an inherent credit or financial risk when issuing a policy in front of an alternative risk arrangement. In order to alleviate this credit risk, the carrier requires the posting of collateral commensurate with 'risk gaps' to ensure appropriate funds are always available to pay claim obligations incurred by the captive. Collateralisation is actually a requirement effectively imposed on carriers by the National Association of Insurance Commissioners (NAIC) as liabilities and ceded risk amounts must be recognised on the insurer's annual reports.

Schedule F is the section of an insurer's annual statement filed with regulators and discloses the insurer's reinsurance transactions. Reinsurance transactions are an obvious and important consideration in determining an insurer's strength and, ultimately, the financial rating it receives.

Every time an insurer writes an account, particularly those associated with most alternative risk arrangements, the corresponding reserving requirements tied to that business will have some diminishing implications to the carrier's surplus ratio. The negative surplus implications can be offset by the portion of risk that the carrier chooses to cede to a qualified reinsurer.

Statutory accounting procedures allow an insurer to recognise amounts of risk ceded to reinsurers as either assets or reductions from liability, which provide a corresponding offset to the surplus reductions associated with writing amounts of insurance business.

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Reinsurers are classified as either authorised or unauthorised. The classification is based on various criteria, however, most weight is assigned to the reinsurer's financial strength and its capacity to assume risk. In order for the reinsurance-offset credit to be recognised in the insurer's annual statement, the reinsurance must be ceded only to an authorised reinsurer. Regulators do not permit Schedule F credit to be taken for reinsurance placed with an unauthorised reinsurer.

Such a transaction would result in a corresponding decrease to the insurer's statutory surplus unless the transaction has been fully secured through acceptable forms of collateral as defined by the NAIC. Approved forms of collateral are cash, evergreen letters of credit (LOCs) or funds held in a Regulation 114 reinsurance trust.

As mentioned earlier, in a fronted alternative risk arrangement, the captive itself is serving as a reinsurer to its issuing carrier for the amount of risk that is retained by the captive. In most cases, the captive is considered to be an unauthorised reinsurer. In order for the carrier not to be 'penalised' for unauthorised reinsurance, full collateralisation for the amount of risk ceded to the captive will be required.

A carrier will usually require collateralisation for the 'gap', which is created by the difference between the amount of funds available to pay claims (loss funds less the internal gross-to-net expense retention) and the point at which reinsurance attaches.

Collateralisation is held until such time as potential claims liabilities, especially incurred but not reported (IBNR) can be determined. The duration can be as little as a few months for short-tail coverages, such as medical stop-loss, to several years for longer-tail coverages such as workers' compensation. As loss periods become actuarially mature and the books are closed on specific plan years, the carrier will be able to begin releasing amounts of collateral allocated to that year, as the full amount of securitisation is no longer necessary.

Common forms of collateralisation

LOCs

LOCs are the most widely used form of alternative risk collateralisation. An LOC is an agreement issued by an accredited bank that guarantees the availability of funds to satisfy a payment obligation. In an alternative risk programme, the payment obligation is created by an issuing carrier ceding risk to a captive.

An LOC agreement has three parties: the issuing bank, the insurance carrier (beneficiary) and the employer or captive (applicant). The LOC is typically issued for a specific dollar amount directly corresponding to the amount of risk ceded from the insurer to the captive. Banks typically require a pledge to cash or highly marketable (liquid) securities from the employer as funding for the LOC. The bank will also charge a fee based on the amount of the secured obligation for issuing the LOC.

An LOC usually needs to be irrevocable and unconditional in structure. An irrevocable LOC cannot be canceled or modified without the agreement of each of the three parties. LOCs typically expire one year from the issuance date. However, most ceding insurers will require an evergreen clause, which automatically renews the LOC for additional terms as required for securing the full duration of the obligation. The amount and terms of the LOC cannot be modified or cancelled without the consent of the beneficiary.

Reinsurance trusts

A second alternative form of collateralisation is a reinsurance trust, which is sometimes referred to as a Regulation 114 trust. A trust is established by the captive and an agreement is entered into between the captive, the issuing carrier and a bank. The bank serves as the trustee for the fund in this type of arrangement. As with an LOC, the insurer is named as the beneficiary and the trust is funded by cash or marketable securities that can be easily converted to cash.

Funds withheld arrangements

Funds withheld arrangements have become increasingly popular in recent years. In these arrangements, the issuing carrier holds the risk premium until all of the captive's loss obligations (claims) attributable to each securitised contract year have been closed. The captive does not typically receive investment returns on the reinsurance premium as it is held by the insurance carrier rather than the captive, to be available for claims.

The carrier releases the reinsurance premium to the captive after the liabilities of the policy period can be closed. Funds withheld arrangements are usually the easiest and most inexpensive method of risk collateralisation.

Alternative risk collateralisation has long been a source of confusion for many captive owners and insurance professionals not having regular experience with fronted captive arrangements.

As more employers look to incorporate captives into their risk and benefits management strategies, an understanding of collateralisation will become increasingly important. **CIT**

> "As more employers look to incorporate captives into their risk and benefits management strategies, an understanding of collateralisation will become increasingly important"

Phillip Giles, Vice president of sales and marketing, QBE North America

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A cool customer

Steve Bauman of Zurich suggests it will be interesting to see how regulators react and begin to craft legislation, controls and requirements around

What are some of the top cyber threats a company faces on a daily basis?

There are a lot of different cyber threats around the protection of data, the privacy of that data and the security of that data. Cyber is such a broad term and people get confused because of how many areas there are. Cyber is just a generic term but security and privacy of data is the main focus of the product.

Are cyber risks coming from within or outside of the company? What are seen as the bigger threat?

Threat vectors stem from all directions. While current employees cause the largest portion of breaches, according to PwC's Global State of Information Security Survey, opinions on whether internal or external actors pose a larger risk varies depending on the responder. External threats, which tend to be malicious and intentional in nature, leverage an army of resources to penetrate company perimeters, navigate the network, and mine for crown jewels.

Conversely, internal threats already reside and know the environment but are harder to detect without strong behavioural analytic tools, because human error may play a role.

How will these cyber threats evolve over the next five years?

I don't think anybody knows. I think what's unbelievable is that cyber is a risk no one in the captive field had on their radar until recently. If you think of where we as an industry are now, and the fact that in the news you hear of cyber breaches nearly every day, I can't imagine where it's going to be in five years.

I know if we don't do anything about it no one is going to be in a good position. I think by recognising that cyber is an emerging exposure and risk, we can keep it under control and begin to do something. Buying insurance is a good way to start the process but I think captive utilisation is the next step and it also makes a lot of sense for many companies.

According to research in 2015, only 1 percent of captive owners were funding cyber risk through their captives. How has this number changed?

Only 1 percent of captive owners in 2015 is a very small number. I guess it's because it wasn't on anyone's radar then or several years ago. I think we're going to see exponential growth in captive utilisation for cyber.

Zurich recently launched its new cyber solution for captives. How does the programme work and how will clients benefit from this?

The new solution marries captive utilisation and the products that insurance companies like ours have in the marketplace. It takes our underwriting expertise, the policy forms and the policy infrastructure that we have and marries that to a captive.

The solutions gives the captive the benefit of having the expertise of the policy form and the ability to tap into the services that Zurich puts out in front of captives. Anytime you mitigate losses going to the captive, that's money saved in the captive and that's underwriting profit that's retained. Captive utilisation accrues to the benefit of the parent owner of the captive.

As you said, cyber was off the radar for companies five years ago. What other emerging risks should companies be looking out for?

There continues to be the emerging risks of compliance, or rather non-compliance, or even lack of compliance. If you think about insurance that is regulated in every country around the world and every state in the US, the possibility or risk of being non-compliant is increasing. Captives really need to pay attention to the environment that they're doing business in, and they need to make sure that the programmes that they are involved in are compliant. The risk of being non-compliant is increasing and that continues to be an emerging risk for captives and their owners as well.

What will be interesting is to see is how the worldwide regulatory bodies look at the cyber threat and how they will craft legislation, controls or requirements on companies and therefore captives to see how that develops. I think it is going to be really interesting.

As more compliance and regulatory bodies look at captives and more of them look at cyber, it will be really interesting to see how that develops. There are some regulatory bodies that are already looking at this issue now. I know the Federal Insurance Office and the National Association of Insurance Companies are both looking at it in the US, as is the International Association of Insurance Supervisors. **CIT**

Steve Bauman
Senior vice president and head of captives
Zurich North America

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Misperceptions add costs to captives

It is disappointing when measures that result from misperceptions add to the administrative costs of operating a captive, says FERMA's Jo Willaert

There are quite widespread misconceptions about captive insurance, and it is important that European tax authorities understand better how captives support European business. This is not about tax, but a fear that the administrative costs of owning a captive will become uneconomic, and companies will lose a valuable tool of enterprise risk management.

The Federation of European Risk Management Associations (FERMA) represents the interests of more than 4,700 risk and insurance managers, and about one-third of them work in organisations that use a captive to manage some risks of their operations.

We are, therefore, trying to dispel misconceptions about captives current among international bodies and tax regulators. We have prepared a position paper on captives that we are first sending to the OECD so that the views of risk managers are taken into account in the discussion on implementation of the base erosion and profit sharing (BEPS) measures. We have also urged our 21 member associations across Europe to use the position paper to approach their national tax authorities, which will be responsible for deciding how to implement the BEPS measures, to explain the real risk management value of captives.

Captives play an important role in increasing the resilience of European businesses. We see this as an important aspect of captive insurance for the Organisation for Economic Co-operation and Development and the EU to understand. Insuring through a captive is not just a transactional exercise in saving money on insurance premiums or getting additional risk capacity not available from the commercial insurance market, although those are incentives.

They focus the mind of management on improving risks, since it is very clear how much losses insured through a captive cost. The captive can provide global loss distributions that allow management to analyse the results and incorporate them into the enterprise risk management process across the company's sites and processes. Reducing the number and extent of losses in this way contributes to the ability of the company to take business risks and so contribute to economic growth.

BEPS, EU anti-tax avoidance and financial transparency initiatives will be the subject of a risk managers-only discussion at the FERMA Seminar in Malta on 3 and 4 October. There will also be a presentation on captive insurance and cells in Malta. For more information, see http://www.ferma.eu/ferma-seminar-2016/

The full FERMA position paper on captive insurance companies is available on the FERMA website at www.ferma.eu

Already the complex Solvency II data analytics and reporting are increasing the cost pressures on captives. We find it ironic that Solvency II was designed to include captives as much as possible as normal regulated insurance companies, despite requests from the risk management community for more proportional regulation.

Now BEPS and initiatives from the European Commission are differentiating captives from the rest of insurance companies.

Proving compliance with the BEPS requirements we believe will add further costs for captive owners. Our hope is that the what we are doing for Solvency II will be instrumental to prove BEPS compliance at moderate additional cost for EU-domiciled captives and, therefore, will be not prohibitive to maintaining a captive.

What we do not know is the extent to which the extra administrative costs will discourage the formation of new captives.

Finally, in light of the latest corporate transparency and anti-tax avoidance measures at the EU level, FERMA will also reach out to the European Commission and Parliament to increase their understanding of the role of captives in the European economy. This follows the adoption in July of the Anti-Tax-Avoidance (ATA) Directive by the Council of the EU.

The treatment of captives under the ATA Directive should also remain consistent and aligned with the Solvency II regime where captive insurance companies are subject to the same regulatory environment in terms of governance, risk and capital as other insurance and reinsurance companies.

FERMA believes it is crucial that tax authorities understand the positive technical risk management aspects that captives can represent for multinational organisations.

Although we are convinced that EU-domiciled captives will pass the BEPS test, the administrative costs of owning a captive are very likely to rise. That will increase the total costs of doing business which is not in anyone's interest. **CIT**

Jo Willaert
President
Federation of European Risk Management Associations

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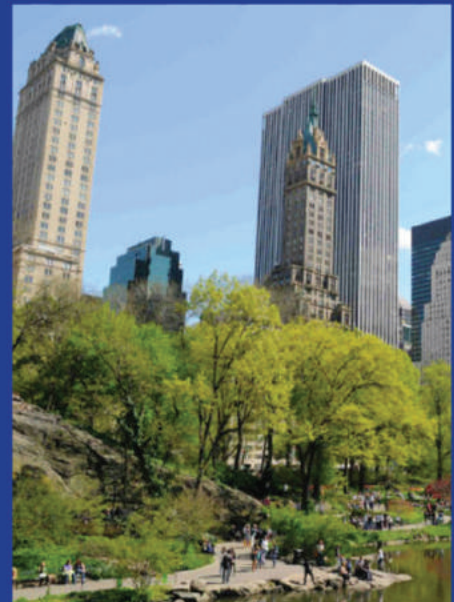

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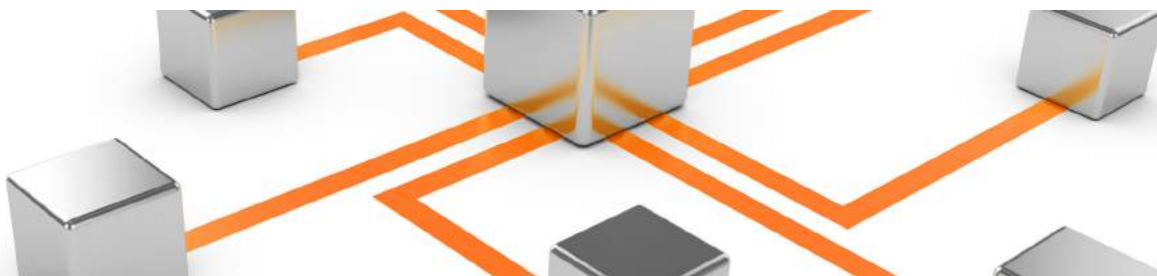

A frank exchange

Exchange Re's John Tortell explains how Malta can become an ILS hub

Exchange Re has received approval for the EU's first SSC platform for cell-based ILS and collateralised reinsurance transactions. How will this work and what do you have to go through to set it up?

Malta is the first EU member state to adapt cell structures for insurance-linked securities (ILS) transactions. Dedicated regulations give certainty to securing capital for insurance entities.

This is the first ILS platform in Malta for private collateralised reinsurance and other ILS transactions organised as a securitisation cell company (SCC).

Exchange Re's segregated cells will be constituted to enter into securitisation transactions. Authorised as a reinsurance special purpose vehicle (RSPV) under the Maltese RSPVs regulations and fully compliant with the EU Solvency II regime, the platform offers lower costs and a quicker set-up time for individual transactions.

Exchange Re invites all managers to populate and manage cells on the platform. This is an independent structure that will allow other managers to manage cells in the structure. The purpose of this is to relieve the managers from the requirement of owning a platform together with the issues of conflict of interest that these may generate.

Market research was done and a niche market exists. Therefore, together with the Malta Financial Services Authority (MFSA), a process was enacted to ensure the application process was initiated and over the period a seamless transition to the market was made.

Do you think the approval of Exchange Re will spur an interest in others to follow suit?

It could be that others follow suit. In an ever-evolving market new solutions are continuously being looked at but first-mover advantage is what we were also looking at.

With time, do you think Malta has the potential to become a European ILS hub?

Definitely. As Malta has become an EU destination for captive entities, we also feel that Malta will also eventually also become a European ILS hub. The regulator has been providing the tools to the market operators, enacting laws that increase the visibility of Malta as an insurance destination.

Over the years, the local market operators, which include all the major international names, have moved ahead with these tools to enhance the local product offering internationally.

Cell creation is subject to regulatory approval and the MFSA is committed to processing applications in line with market-standard timeframes that are established with applicants beforehand. This business approach of the MFSA is crucial to the whole process.

The benefits of cells in the SCC include: a market-friendly authorisation process; cost-efficient structure; Solvency II-ready; managed or self-managed; tax neutral irrespective of funding model; all benefits of the Securitisation Act, for example statutory bankruptcy remoteness; and robust legal structure and segregation. These are all important if Malta is to become an EU ILS hub.

What more does Malta need to do to achieve a European ILS hub status and compete with the likes of Cayman and Bermuda?

The importance is credibility from all the service providers' side and speed to market from the regulator. Malta needs to compete with the likes of Cayman and Bermuda to become an ILS hub that can provide an alternative cost-effective efficient solution. Being EU-based can add to the attraction for operators that need ease of access to markets.

In five years, where do you see Malta's ILS market?

We see that EU companies would want to be located in the EU especially with the increasing compliance requests and ease of access. With some cells being authorised, one will be able to test the benefits of the scenario and will therefore push more arrangers, sponsors and brokers to use the domicile for their transactions. CIT

John Tortell
General manager
Exchange Re SCC

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Potent potential

Danielle Hermansen of PKF Malta discusses how Malta can and is fully utilising its potential in the insurance industry

PKF Malta will participate in the New York Captive Owners Summit, planned to take place on the 31 October 2016 in New York. This is a sequel event, under an innovative, more intimate setting, especially created for America's leading captive owners.

FinanceMalta, being at the forefront to stimulate investment, believes this initiative will help Malta in its quest to remain a compelling proposition for prospective investors seeking to establish or extend their footprint in Europe. The New York Captive Owners Summit is a highly exclusive learning and networking event, centered around a series of in-depth roundtable sessions.

A previous event was organised on 29 March 2016, with the support of FinanceMalta, Bee Insurance Management and a host of keynote speakers, in New York, promoting captive insurance opportunities for the US market. This was the first Malta-focused event of its kind, seeking to attract US companies to host their European captives in Malta.

Topics included: how to survive the Foreign Account Tax Compliance Act and Common Reporting Standard; what regulations one should look out for; and finally, the advantages that Malta offers as a domicile that continues to strengthen its position in Europe as a strong player in the captive market. Developed over a decade of continued building of the country's financial services infrastructure and legal framework, this makes the operation of captives more attractive on this island. The jewel in Malta's crown is the protected cell company (PCC). Malta is the only full EU member state that can offer PCCs. Malta is also the only EU member state that offers the securitisation cell company structure used for asset-backed financing or insurance-linked securities platforms.

The insurance market is experiencing a dramatic change in culture, mainly due to the aftermath of Solvency II. While many are entwined with allocating their resources to complete the QRTs and thematic reviews, a survey carried out on the local market shows that 57 percent of local insurers, have been somewhat surprised at the magnitude of additional effort necessary to be compliant for Pillar III relative to the time available. The XBRL converting issue is one of the main factors that locally contributed to additional difficulty in meeting the deadlines.

Without any doubt, one of the key advantages of Malta remains our geographical disposition. This is an attraction to multinational operators and to a number of household names in the risk management industry. Malta has managed to prosper from being small, thus affording to give the flexibility and accessibility with a stronger customer focus. At PKF Malta we pride ourselves in being the right size to provide the right solutions with the right people. This is evidenced in the assistance our team of insurance, tax, finance and legal experts may provide during a company's feasibility, pre-licensing and licensing process and as well throughout an entity's ongoing operation.

We provide value adding recommendations and have assisted clients in embedding risk management processes into their day-to-day operations. The first year of reporting will be challenging for insurers as they get to grips to the Solvency II requirements. PKF is able to provide expert advice to help insurers and/or start-ups face up to these financial reporting challenges. As service providers, we place value on the relationship we build with our clients. We believe that, by basing a relationship on trust, we can provide clients the best tailor-made service possible.

We endeavour to provide our clients with the right combination of skills, experience, statistical methodologies and programmes to deliver the assurance and support their need.

PKF is committed to train our staff to enable them to provide client service of the highest standards. Professional staff proposed for respective projects are closely involved throughout the work and provide main source of continuity. A number of key experts enable delivery of all the objectives in a timely manner.

The company has an insurance team providing specialised services to the insurance industry. Licensed by the Malta Financial Services Authority as an approved auditor in carrying out external audits to insurance companies and insurance intermediary companies, it works closely with specialised service providers within the local industry to cater for clients' needs including set-up arrangements. Being an integrated member firm of PKF International, it also teams up with overseas offices to deliver specialised technical solutions to the local insurance industry.

It is worth noting that in the EU there has been a plateauing effect experienced by the captive market, which is mainly be attributed to uncertainty due to the complex rules of Solvency II. The learning curve has been great, however, the benefits are starting to be felt within the market and undoubtedly there is a window of opportunity to refocus again on market development. Recent developments in the EU insurance industry are also characterised with topics on Brexit and its possible ramifications.

PKF Malta has seen the potential of the growth in the US market, and the need for this market to have somewhere to overspill, as US firms set up in Europe to insure their European risks. This has become poignant in the need for multinationals to insure their employee benefits through their captives. It's a difficult task that is however becoming more possible than ever, with the benefits beginning to make a difference in balance sheets. **CIT**

Danielle Hermansen
Director
PKF Fiduciaries
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Natural neighbours

The Pacific Catastrophe Risk Insurance Facility Act provides insurance coverage benefits and enhances opportunities in the region, says Tamatoa Jonassen

The Cook Islands was selected as the domicile of choice for the Pacific Catastrophe Risk Insurance Facility (PCRIF) based on its well-established international financial services sector, and the strength of its regulatory regime and implementation of international standards.

In June of this year, the Cook Islands passed the Pacific Catastrophe Risk Insurance Facility Act 2016 with the purpose of establishing a legal framework for the PCRIF, facilitating the funding thereof, and allowing participating Pacific island countries greater management of disaster and climatic risk financing on the regional level.

The PCRIF established under the act is essentially the continuation of a Pacific catastrophe risk insurance pilot programme launched in January 2013. The pilot programme is a product of an initiative from 2007 designed to provide Pacific island countries with disaster risk assessment and financing tools to allow enhanced disaster risk management and climate change adaptation. The initiative's progress was made possible through the collective efforts of the World Bank, Asian Development Bank, Pacific Islands Forum Secretariat and the Secretariat of the Pacific Community Applied Geosciences and Technology Division with financial support from the government of Japan, the Global Facility for Disaster Reduction and Recovery and the EU.

A number of countries have pledged financial commitments towards expanding the initiative, including Germany, the UK, US, and Japan, with some of those commitments formally announced during the Paris COP21 climate negotiations in December 2015. Similar disaster risk management initiatives are also ongoing in the Caribbean and African regions, namely the Caribbean Catastrophe Risk Insurance Facility and the African Risk Capacity.

The continuation of the pilot programme into the PCRIF allows participating Pacific island countries to continue receiving the benefits of the pilot programme and access to regional risk pooling mechanisms to secure insurance coverage for natural disasters through the international reinsurance market at competitive prices. With the aim to increase the financial resilience of Pacific island countries and improve capacity to quickly meet funding needs due to major disasters, the programme provides direct support to governments of participating Pacific island countries to finance immediate disaster relief and provides advisory services relating to public financial management of disasters.

The programme has already provided disaster assistance over the past three years and paid out approximately $3.2 million to participating Pacific island countries in relation to natural disasters. In January 2014, Tonga was paid $1.27 million after the impact of Cyclone Ian, while in March 2015 Vanuatu was paid $1.9 million in the aftermath of Cyclone Pam. The insurance coverage provided under the programme covers some portion of major disaster losses, which may include losses related to a disruption of central government operations and basic public services, but is unlikely to be used for low disaster losses from frequent and less severe disaster events where risk-retention mechanisms such as contingency budgets and national reserves are maintained by participating Pacific island country governments.

The current participating Pacific island countries are the Cook Islands, the Marshall Islands, Samoa, Tonga and Vanuatu. With the establishment of the legal framework under the recent act, it is anticipated that more Pacific island countries will join PCRIF.

The act establishes PCRIF by capitalising on legislation for foundations and captive insurance already in place in the Cook Islands. Enacted this year with bipartisan support, the act forms two legal entities.

The first legal entity is the Pacific Catastrophe Risk Insurance Foundation administered by a council of members consisting of each participating Pacific island country and four members representing developing partners. This structure ensures that all participating Pacific island countries have ownership over the management of PCRIF while those partners contributing to the establishment of PCRIF maintain input in ensuring its purposes are met.

The rules of the foundation allow for the appointment of an enforcer, similar to the role of a protector used in international trust structures, which may be given functions or powers under the rules of the foundation. Such enforcer functions could include powers to direct or disapprove certain specified actions of the council, adjudicate council member disputes or matters of interpretation relating to foundation rules, or even require the production of financial statements and accounting of foundation assets.

The Cook Islands Foundations Act 2012 requires that if an enforcer is appointed in a foundation that such enforcer take reasonable steps to ensure that the council of a foundation carries out its functions. The option of having an enforcer allows for additional safeguards in ensuring the purposes of PCRIF are fulfilled.

The second legal entity established under the act is the Pacific Catastrophe Risk Insurance Company with its ownership resting

solely with the foundation. The insurance company is to be licensed under the Cook Islands Captive Insurance Act 2013 and allows it to undertake captive insurance business for the benefit of PCRIF's participating Pacific island countries.

While the foundation ensures sustained support from all stakeholders by providing them with representation on the foundation's council, the insurance company is able to focus on insurance-technical decision making, which minimises political interference risk to business operations.

Together with the act, the foundation and insurance company provides the structure for PCRIF to be administered and regulated from the Cook Islands. The Cook Islands's financial services industry is regulated by the Financial Supervisory Commission, and the strength of its regulatory framework is reflected in the meeting of international standards. In 2009, the Cook Islands was positively evaluated by the Asia Pacific Group on money laundering, a Financial Actions Task Force style regional body, resulting in the Cook Islands being in the top 20 percent of the 165 nations assessed for implementing international regulatory standards.

Positive evaluations were also given in both peer review phases by the Global Forum on transparency and exchange of information for tax purposes, with the second phase report published in 2015. The Cook Islands has also committed to the automatic exchange of information and anticipates the common reporting standard to be fully implemented by 2018.

The World Bank and its partners have played a vital role in the realisation of PCRIF being established and domiciled in the Cook Islands. The selection of the best domicile was carefully considered where legal and regulatory framework also allowed for flexibility and stability. With the assistance of financial contributions from donor countries, the formation of PCRIF is arguably the most cost-effective option for sustainable parametric insurance coverage for disasters in the Pacific that still ensures ownership over management of PCRIF is retained by participating Pacific island countries.

Furthermore, in addition to the benefits of insurance coverage reducing the financial vulnerability of Pacific island countries to natural disasters, the establishment of PCRIF further enhances opportunities in the Pacific region towards building technical insurance expertise and support. CIT

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CEO
Cook Islands Financial Services
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A new take on claims management

Captives and risk managers need to be in control of their claims processes and information flows, according to Gwenny Nales of Van Ameyde

Captives and risk managers dealing with the risks of multi-office and often international companies share a major problem: fragmented data, requiring structural data cleansing and making data analysis virtually impossible. International claims and insurance processes invariably result in multiple flows of information that are difficult to manage in terms of accuracy and consistency. Language and cultural barriers, different reporting formats and the heterogeneous nature of the service providers involved only add to the confusion. The lack of overview hampers compliance and risk management, not to mention cost control.

Willem Van der Hooft, business development director at Van Ameyde, explains: "Captives, fronting companies, brokers and risk managers all face similar problems. They have to spend valuable time reconciling data from different sources, in order to establish a reliable basis for decision-making processes, financial reporting and compliance."

"And don't underestimate the risk of fraud and cybercrime posed by the use of multiple sources and platforms. After all, data security is as strong as the weakest link. With so many sources of information it is hard to centrally establish the validity of data, and thoroughly securing different platforms is probably even harder."

Multi-office companies, and companies with international presence in particular, face a host of insurance-related issues. TPML insurance, for example, requires an international network of claims representatives and correspondents, to deal with claims under the Green Card regulations and EU Directive 2009/103/EG, still referred to by many as the Fourth Directive. The parties involved include fronting companies, preferred supplier and repair networks, third-party administrators (TPAs), claims adjusters, the police and hospitals. All these parties provide their own flows of information using their own platforms.

Michael Akerboom, business development manager at Van Ameyde, says: "Insurance providers in general struggle with their reporting and reporting departments mushroom as compliance with ever stricter regulations require a level of transparency that the information provided by all those parties does not provide. I see a huge potential for efficiency gains."

Akerboom distinguishes three main purposes of reporting. The first is the management of suppliers, based on service level agreements and the agreed key performance indicators. Captives need to be able to monitor the performance of their suppliers and fronting companies have similar monitoring needs.

The second purpose is risk management. Management information must provide insight in all aspects of losses, including the cause in order to identify potential for mitigation, and, of course, claims costs. Management information provides the basis for risk management decision-making and is one of the areas in which the captive can clearly establish its added value to its owner.

Regulatory compliance, such as Solvency II, is the third purpose of reporting. Insight in outstanding liabilities requires correct and uniform reporting of claim reserves. In addition, tight deadlines and strict reporting requirements put a strain on reporting departments faced with the task of data cleansing.

Reducing costs

Reducing claims costs is another major issue in the insurance industry. Prevention is one of the pillars, but in order to prevent losses, the cause of losses must be identified. Akerboom explains: "If, for instance, a motor fleet could considerably decrease its losses by installing reverse radar in its cars, the fleet manager needs to know that so many of the fleet's losses are related to vehicles backing up."

"Another major cost influencer is loss recovery, or, in fact, the lack thereof. We see the same issue across the board. There is no process in place to ensure that the necessary steps are taken towards all liable third parties. Systems are simply not geared to the registration, identification and processing of such recoverable losses."

A single platform

The answer is to move to a single, international claims and incident management platform. By using a single platform, not only is the need for data cleansing eliminated, but costs can be reduced demonstrably as well, thanks to efficiency gains, automatically initiated loss recovery and automated fraud prevention.

In Akerboom's opinion, ideally all losses—irrespective of the type of loss—from multiple territories are notified using an online and mobile portal. The portal is connected to a central claims management system, which triages the losses to the parties involved and identifies recoverable losses. All parties involved use the portal for reporting by means of standardised reporting templates, thus converging all information flows and presenting the information in a customised, uniform format resulting in a unified overview.

Collecting all the data in one system also offers potential for data analytics for a wide variety of purposes. Data analytics can be used for studies into claims cycle times, cost effectiveness and fraud prevention, but also for gaining insight in causes of loss for risk analysis and mitigation purposes. And finally, when it comes to safeguarding data, one central system can be defended to the hilt.

Van der Hooft notes that the problem faced by captives and fronting companies, is the fact that this would require huge investments in

claims management IT, rather than in their core business. Yet most captives and fronting companies do not deal with the vast number of claims that would justify such investments: they do not have the scale for the development and cost effective operation of such a platform.

Conversely, TPAs do have the scale but most only develop functionality to support their own services. A number of systems are available on the market, but systems that cover the whole process are scarce. Akerboom suggests: "Today, claims management fully depends on IT support, which is why Van Ameyde has its in-house IT company that develops all functionality based on service-oriented architecture."

"This enables the development of agile systems that can be adapted easily to each customer's needs. The process of loss notification and triage that I described is covered entirely by our Incident Management System (IMS). IMS was initially developed to meet the needs of a global car rental company, but now serves a wide variety of clients."

Investing versus outsourcing

By outsourcing the development of a customised IT platform and the claims management services to a single TPA, the reporting and cost control issues can be solved, without having to make huge investments in the captive's or fronting company's non-core business.

Of course, choosing the right service provider presents its own set of challenges. The service provider needs to be able to prove the reliability of its processes and systems, for instance by means of ISAE 3402 certification. ISAE 3402 is an assurance standard that covers procedures, controls and information security. The IT platform must be able cover the desired territories and a dedicated network of offices must ensure the quality of claims management and loss recovery.

Service levels need to be defined in terms of key performance indicators on the basis of which the service provider's performance can be monitored.

Investing or outsourcing remains a strategic choice. One thing is clear though: captives and fronting companies must gain control of their claims processes, and the use of a single platform across the territories to be covered provides the optimum solution. **CIT**

Gwenny Nales
Manager of
corporate communications
Van Ameyde

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Becky Butcher reports

A new journey

The new CEO of DIMA, Eddy Van Cutsem, says there is a lot still in store for the association over the course of the year, and in 2017

What's going on at DIMA right now, and what's new?

I started in the CEO role on 1 August, so it is still early days, however, I have been in the reinsurance industry for many years as CEO of a European captive manager and as managing director of a reinsurance subsidiary owned by a North American bank. I have also had a direct involvement with the Dublin Insurance & Management Association (DIMA) over the years. I was one of the founders of the association, a board member and vice chairman, and therefore I'm very familiar with DIMA as a representative body and its activities.

My first task as interim CEO is to get up to date as quickly as possible and also to ensure continuity from where Sarah Goddard departed. Further down the line, we have quite a lot of things planned for our members in terms of training and education, and we also are looking ahead to our 2017 European Insurance Forum, which will take place on 25 May next year.

As interim CEO at DIMA, what are you currently working on?

Una Coleman, our education manager, is organising a number of projects that will come to fruition in the autumn. These include technical briefings and briefings in terms of new developments and the insurance market. Also, Solvency II will remain a big topic. Although it has been embedded in the regulatory environment, there are still new and technical aspects coming up as a result of its implementation. There are also emerging risks including cyber and Brexit.

At DIMA, we are expecting that there will be more clarity in the next few months on what happens with Brexit and what it means for not just the UK but also for Ireland and the rest of Europe.

In Ireland, have you seen any concerns from insurance companies around Brexit?

It is still early days and UK-based companies are trying to establish what they need to do and DIMA will obviously help them where we can in terms of finding information that they require.

If they want to they can meet with myself or member companies that have an operation here and they can share experiences.

In the meantime, I understand that UK-based companies are looking at contingency planning for a worst-case scenario because the loss of freedom of services in the EU, would become a reality.

DIMA will also contribute to the implementation of what is called IFS2020, which is the Irish government's strategy for further developing the international financial services sector in Ireland. International reinsurance and insurance is one of the pillars.

A strategic group was set up, which has been put together by the government and works across all internationally focused financial sectors to develop the financial services sector and create jobs in Ireland. DIMA will focus on the international insurance and reinsurance side.

Since the implementation of Solvency II, have you seen much of an impact on captives? Have members informed you of any challenges they are facing?

The challenge for captives is the complexity, the workload and the resulting operational cost of implementing the Solvency II requirements. Solvency II does not allow enough room for the application of proportionality for captives and smaller companies.

Hopefully, the upcoming review of Solvency II in 2017 and 2018 will address this issue, as well as others.

Many countries will be expected to subscribe to the BEPS framework put together by the OECD. Are there any implications for captives following the framework?

DIMA is monitoring the development of the BEPS framework and its impact on the industry. The impact will depend very much on the group structure under which the captive is operating as well as the domicile of its shareholders. So far, the impact on captives based in Ireland has been very limited, if any.

And finally, are there any future plans in place to appoint a permanent candidate for the CEO position at DIMA?

I will be in this role for now and there is no timeline currently in place to appoint a permanent CEO.

One of my main tasks as interim CEO is to look strategically at what DIMA is doing and how it can improve its offering to members, which is one of the main reasons why I was hired.

Hopefully by doing this it will help to increase our membership and its revenues. CIT

> "The impact of the BEPS framework will depend very much on the group structure under which the captive is operating as well as the domicile of its shareholders"

Eddy Van Cutsem, CEO, Dublin Insurance & Management Association

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Matthew Carter has joined JLT Re as a partner of the London market and international division.

Carter will lead structured and non-traditional reinsurance for the UK and Europe as well as working with the JLT Re structured products teams in North America.

Prior to his new role, he served at Guy Carpenter as senior vice president in the structured products and capital solutions team.

Bradley Maltese, deputy CEO of JLT Re for the UK and Europe, said: "We are delighted Matthew Carter is joining the team, his knowledge and experience of non-traditional reinsurance products such as multiline aggregate contracts, retrospective covers, internal retention vehicles and capital efficiency, is perfectly aligned to our focus and growing client demand in these areas."

The National Association of Insurance Commissioners (NAIC) has appointed Peter Hartt, director of the New Jersey insurance division, as the new state insurance commissioner representative on the Financial Stability Oversight Council (FSOC).

Throughout a two-year term in the role, effective from September, Hartt will represent New Jersey regarding the interests of insurance regulators on the FSOC, a 15-member body comprised of chief financial regulators in the US.

John Huff, NAIC president and Missouri insurance director, commented: "The NAIC and state insurance regulators will be well-served through the selection of Peter Hartt."

"His sound judgment and expertise will be a valuable asset to the proceedings of FSOC as they review systemic risk in the financial sector."

Huff served as the state insurance commissioner representative on FSOC for two terms.

Hartt will replace the North Dakota insurance commissioner Adam Hamm when his term expires in September.

Hartt said: "I am honoured to have been selected by my fellow regulators to represent state-based insurance regulation. I assume this role with great respect for what commissioner Adam Hamm and director John Huff accomplished in their terms."

He added: "I look forward to working with the other financial regulators to promote a stable insurance marketplace and protect the broader financial sector."

Allianz X, the insurance technology specialist company of Allianz Group, has appointed Peter Borchers as CEO, effective 1 October.

Borchers will join from Deutsche Telekom.

Christof Mascher, member of the management board of Allianz SE and COO of Allianz Group, said: "Allianz X will unlock strategic growth opportunities for Allianz in InsurTech and adjoining areas like blockchain, artificial intelligence or virtual reality, addressing topics like mobility, health and care."

"Peter Borchers has broad experiences in digitisation and I am glad he'll join Allianz."

Solmaz Altin, chief digital officer of Allianz SE, added: "We share with Borchers the same enthusiasm about the digital potential in insurance. Allianz X will open up significant growth potential for Allianz in a targeted manner and with creative freedom." CIT

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