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The primary source of global captive insurance news and analysis

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Illinois captive reform vetoed

A bill that could provide a landmark captive framework reform in Illinois has been vetoed by governor Bruce Rauner.

The governor was in support of the updates to the Illinois' captive insurance regulatory structure, but vetoed SB 1737 due to the "concerning" regulatory barriers the legislation imposed on short-term limited-duration health plans (STLDs) and workers' compensation insurance.

The bill proposed a number of amendments to Illinois Insurance Code's regulatory framework, which would provide a substantially improved environment for companies looking for captive solutions, following the lead of jurisdictions like Vermont, Hawaii and South Carolina.

It would give the Illinois Director of Insurance the broad authority to set minimum capital and surplus for captives licensed in the state, based on the amount of premium written, the type of assets held by the captive, the terms of reinsurance arrangements, the types of business covered in policies issued by the captive, the underwriting practices and procedures of the captive, and any other criteria that is deemed to have a significant impact by the Director.

According to the bill, the capital and surplus requirements must not be less than $250,000 for pure captives, $500,000 for industrial insured captives, and $750,000 for association captives.

The bill also permitted captives to meet the minimum capital and surplus requirements using Illinois bonds, US-backed securities or an irrevocable bank letter of credit approved by the Director.

SB 1737 authorised captives in the state to write insurance that covers the risks of a 'controlled unaffiliated business', an unaffiliated entity with whom an affiliate of the captive has a contractual relationship, and the risks of a captive's affiliates.

Captives would also be authorised to issue contractual reimbursement policies to affiliated certified self-insurers—as long as they were authorised under the Illinois Workers' Compensation Act or an analogous law of another state—and to affiliates insured by workers' compensation insurance policies with a negotiated deductible endorsement.

The bill also offered enhanced lending flexibility to Illinois-licensed captives, providing that the captives may make loans to their affiliates.

Additionally, it authorised captives to accept risks from and cede risks to, or take credit for, reserves on risks ceded to an approved affiliated captive insurer or captive reinsurance pool–with the approval of the Director.

The bill, which passed by the Illinois General Assembly on 31 May 2018, also proposed a drop in the premium rate on self-procured insurance from 3.5 percent to 0.5 percent of gross premium. It had the support of the state's Department of Insurance, key industry groups, and multiple large Illinois-based taxpayers.

In the Governor Amendatory Veto Message, Rauner suggested portions of the legislation were "both necessary and wise" and recognised that it updated the captive law "to be more attractive to companies that use that insurance option" and to be "in line with other states, and will help Illinois overcome its competitive disadvantage in attracting the companies that offer this product to Illinois businesses".

Rauner recommended a number of specific changes, mostly referring to the restrictions he felt it placed on STLDs and workers' compensation insurance.

He said: "With these changes, Senate Bill 1737 will have my approval."

International law firm McDermott Will & Emery had strongly supported the enactment of the bill, which they said was "an important and exciting development for the captive community".

In a blog post, McDermott counsel Thomas Jones, alongside partners Lisa Kaderabek and Mary Kay McCalla Martire, explained: "Illinois' underdeveloped captive law and its high self-procurement tax rate have meant that Illinois has never been a viable option as a captive jurisdiction."

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Editor: Becky Butcher
beckybutcher@blackknightmedialtd.com
+44 (0)203 750 6019

Deputy Editor: Barney Dixon
barneydixon@blackknightmedialtd.com
+44 (0)203 750 6026

Junior Reporter: Ned Holmes
nedholmes@blackknightmedialtd.com
+44 (0)203 750 6022

Contributors: Jenna Lomax and Ben Wodecki

Associate Publisher/Designer: John Savage
johnsavage@captiveinsurancetimes.com
+44 (0)203 750 6021

Publisher: Justin Lawson
justinlawson@captiveinsurancetimes.com
+44 (0)203 750 6028

Office Manager: Chelsea Bowles
+44 (0)203 750 6020

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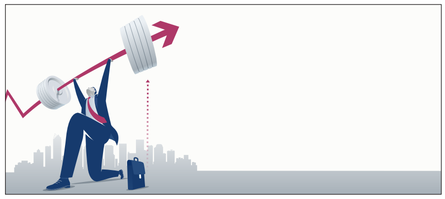
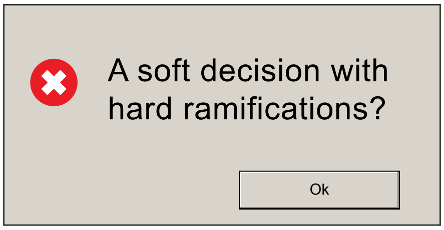




Pareto and R-Health partner for enhanced EB primary care

Pareto Captive Services and R-Health have launched a partnership to bring enhanced primary care to Pareto's clients. The partnership brings together R-Health, a national leader in enhanced primary care, and Pareto, which specialises in forming and managing employee benefits group captives.

The two Philadelphia-based companies aim to cooperate to address the need to provide innovative solutions in tackling ever-rising healthcare costs facing employers and individuals.

The collaboration will provide Pareto clients with access to R-Health's increasing number of direct care practices.

The two companies are partnering to launch two direct care locations in the Kansas City area in September 2018 and plan to open four new practices in the Greater Philadelphia area in 2019, with others locations opened depending on demand.

Mason Reiner, R-Health co-founder and CEO, commented: "By partnering with Pareto, we can leverage our unique combination of clinical expertise and technology to provide patients with consistent access to their personal doctor while achieving significant cost savings for employers through clinically integrated care delivery and innovative data analytics."

Pareto managing director Andrew Cavenagh said: "Pareto saw that our captive members needed a better primary care option for their employees, yet for most medium-sized employers, on-site clinics are not financially feasible and, often, can lead to further fragmented care."

He continued: "By partnering with R-Health to create near-home practices, we can fill that void by offering better access to primary care and more time with their physicians. These offices offer convenient and comprehensive primary care to employees and their family members."

LIIBA proposes post-Brexit equivalence regime for insurers

The London and International Insurance Brokers' Association (LIIBA) has proposed that the UK Government seek a workable equivalence regime for insurers in Brexit negotiations.

In a letter sent on 22 August to UK prime minister Theresa May, LIIBA chairman Roy White said the association was concerned that any agreement by the government to an enhanced equivalence regime will create uncertainty for insurance intermediaries.

White wrote: "We have noted the proposals the government has made in its White Paper for trade arrangements for financial services after the UK leaves EU."

"As you will be aware, there is no equivalence framework either under Insurance Mediation Directive nor Insurance Distribution Directive (IDD), which comes into force on 1 October."

"Clearly in the absence of an existing equivalence regime, enhancements will not work."

The letter explained that the government should seek an equivalence regime similar to the regime enjoyed by investment managers under the Market in Financial Instruments Regulation, which allows firms to provide services to professional clients in the EU provided they are registered with the European Securities and Markets Authority.

Investment firms do not need to have an establishment in the EU under this regime.

According to LIIBA CEO Christopher Croft, the buyers of insurance must not be the unintended victims of Brexit.

Croft explained: "Major EU corporations could be faced with profound consequences post-Brexit without access to London insurance."

We need to find a way of maintaining client access to the specialty expertise in London that allows us to provide the cover that simply could not be sourced anywhere else."

"The government's white paper provides a measured foundation from which the right future trade agreement for financial services can be built."

"We understand in general why that focuses on the existing equivalence regimes but our relevant directive—IDD—has no such concept."

He concluded: "We are keen to work with the government to help find a pragmatic way forward."

PartnerRe fined €1.5 million by Central Bank of Ireland

Dublin-based insurers PartnerRe Ireland Insurance dac (PRIID) and Partner Reinsurance Europe SE (PRESE) have been reprimanded and fined a combined €1.54 million by the Central Bank of Ireland.

PRIID was reprimanded for a total of six breaches and PRESE a total of three breaches of Solvency II and the Corporate Governance Requirements for Insurance Undertakings 2015.

The breaches were admitted by PRIID and PRESE, both of whom are Dublin-based entities of PartnerRe, and occurred from the inception of the Solvency II regime on 1 January 2016. Remediation continued up to 30 May 2018.

The breaches were related to PRIID and PRESE's failings in corporate governance frameworks, which resulted in breaches of the Solvency II regime relating to the calculation of their Solvency Capital Requirement for 2016, and the submission of incorrect information to the Central Bank in respect of their solvency for 2016.

A statement from a spokesperson for PartnerRe said the company has taken full responsibility for the errors it made.

The spokesperson stated: "While both companies were at all times solvent and policyholders were never at risk from an economic perspective, mistakes were made in the 2016 quarterly filings by each company."

"On discovering the discrepancies, the companies immediately reported the issue to the Central Bank and acted swiftly to remedy the situation."

"They also initiated an independent third party review and have since implemented recommendations for improving their internal controls and reporting processes for Solvency II."

"While disappointed to have fallen short of our own high expectations, we are pleased that the investigation has now concluded and the Central Bank has indicated its satisfaction with our remediation efforts and our improved governance and processes."

Seána Cunningham, director of enforcement and anti-money laundering at Central Bank, said the actions taken demonstrated the importance that the bank puts on firms meeting their regulatory obligations under Solvency II and the Corporate Governance Requirements.

Cunningham explained: "The Central Bank's investigations found that PRIID and PRESE submitted regulatory returns to the Central Bank, which overstated their solvency positions."

"This was due to both firms incorrectly calculating their Solvency Capital Requirement."

"As a result, both entities were required to re-submit their regulatory returns to the Central Bank."

"This revealed that they had, not only presented the Central Bank with an inaccurate picture of their respective solvency positions but also in the case of PRIID, it resulted in a breach of its Solvency Capital Requirement."

Cunningham continued: "The Central Bank believes that PRIID and PRESE failed to put in place sufficient processes to identify and report the risks to which the firms were exposed in respect of their Solvency Capital Requirements."

"As a result, the boards of both firms were not provided with comprehensive and timely reports regarding the calculation and maintenance of their Solvency Capital Requirements."

"Therefore, the boards were unable to fulfill their responsibility and take the necessary action to prevent the Solvency II breaches that occurred."

According to Cunningham, the investigation also found that PRIID and PRESE "failed to design and operate appropriate internal controls to ensure the accuracy of their Solvency Capital Requirement calculations and the monitoring of the Solvency Capital Requirements in line with the stated risk appetite".

"These failings resulted in inaccurate reporting of information to the Board and the submission of inaccurate information to the Central Bank in respect of their Solvency Capital Requirement and, ultimately, the firms' failure to identify the decrease in their Solvency Capital Requirement."

Nevada DOI receives first association health plan filing

The Nevada Division of Insurance has received the first fully-insured association health plan (AHP) filing for the Henderson, Boulder City and Latin Chambers of Commerce in Nevada, following the final rule issued by the Department of Labor (DoL) in June.

The AHP, which will become effective 1 September 2018, is designed for small businesses that are interested in the state.

AHPs are group health plans that allow small employers access to the regulatory and economic advantages available to large employers, by allowing them to be treated as a large group health plan for the purposes of the Affordable Care Act.

Additionally, the DoL's ruling in June allows AHPs to be formed based on a geographic test, such as a common state, city, county, or a metropolitan area across state lines. The rule will also allow working owners without employees to join.

The Congressional Budget Office estimates that four million Americans, including 400,000 who otherwise would lack insurance, will join an AHP by 2023.

Phil Giles, vice president of sales and marketing at QBE North America, suggested the rule may have a future impact on the medical stop-loss captive market but not for three to five years.

He explained: "Once the self-insured AHPs first establish appropriate solvency and credibility, the market should see a fairly significant number placing medical stop-loss into a captive."

Barbara Richardson, Nevada insurance commissioner, described the announcement as "exciting news for Nevada".

She said: "It provides additional insurance options for Nevadans which may fit their personal needs and the needs of their families."

"Not only does it comply with Nevada's health insurance market requirements but it also creates a more competitive small group market."

HIIG and Energi to partner on captive energy solution

Houston International Insurance Group (HIIG) has entered into a partnership with Energi Insurance Services to provide a captive insurance solution for energy clients in need of alternative insurance coverage.

The captive, eCaptiv, is based in Vermont and funded by client participation. Its coverages are auto liability, general liability, excess liability, and workers compensation.

Significant excess reinsurance will be provided above captive retentions.

Stephen Way, chairman and CEO of HIIG, commented: "We are pleased to have reached this agreement in principle with Energi and look forward to working with their very experienced management team and captive clients in building a best-in-class facility."

Brian McCarthy, CEO of Energi, added: "We are pleased to have HIIG as our partner for the energy group captive programmes.

BevCap improves EB offering with Reflexion partnership

BevCap Management, a programme manager for captive insurance companies, has formed a strategic partnership with virtual physical health company, Reflexion Health.

The partnership means that BevCap clients across the US will have access to Reflexion's cloud-based clinical services network and its Food and Drug Association-cleared Virtual Exercise Rehabilitation Assistant (VERA), a digital platform that enables clinicians to remotely monitor patients.

BevCap's client roster, which includes beverage distributors, dairy and food processing, automotive services, and beer wholesalers, will all offer VERA through their employee benefits package.

According to Joseph Smith, CEO of Reflexion, the partnership represents a new market for the company and is the first partner to use its clinical services network to augment VERA.

Smith commented: "Self-insured employers are often leading the charge in adopting convenient, patient-centered digital health technology and services."

"We're excited to offer employers the most complete alternative to traditional physical therapy that delights patients and reduces costs."

Lee Anne Klas, senior account executive of BevCap, said: "The onboarding of Reflexion's VERA platform and clinical services network is an important addition to BevCap's benefits package, which offers clients and their employees a convenient solution to receive consistent, quality care at home following total joint replacement surgery."

"All of our clients in 17 states will benefit from the availability of VERA through this new and improved employee benefits package, and we are confident that this addition will be a tremendous asset to their employees."

Maxseguros 'excellent' ratings affirmed

Maxseguros EPM has had its financial strength rating of A- (Excellent) and the long-term issuer credit rating of "a-" affirmed by ratings agency A.M. Best.

Maxseguros is a single-parent captive insurer wholly owned by Empresas Publicas de Medellin (EPM), which provides reinsurance to the EPM group, covering property damage and business interruption, commercial crime, directors and officers, and construction liability exposures.

The ratings reflect the captive's balance sheet strength, categorised by A.M. Best as strongest, as well as its adequate operating performance, neutral business profile and appropriate enterprise risk management.

Additionally, they are reflective of Maxseguros' strong risk-adjusted capitalisation coupled with conservative balance sheet strategies, as conservative investment policy and limited premium risk exposure.

The ratings also recognise the support of the captive's parent, EMP, which is owned by the Colombian municipality of Medellin and is the largest power generation and multi-utility company in Colombia.

According to the ratings agency, the positive rating factors are offset partially by Maxseguros' limited business and market scope, which is somewhat mitigated by the company's stable results, favourable geographic spread of risk and the history of the captive's growing surplus position, as well as its ultimate parent, EPM.

A.M. Best added: "Additionally, while Maxseguros depends on reinsurance, EPM's senior management is involved intimately in the captive's operations."

The outlook of these ratings is stable, due to Maxseguros' ability to maintain a strong level of operating performance as a result of its demonstrated risk management expertise and conservative underwriting criteria.

In both 2016 and 2017, this held true and the company presented net claims while also producing constant positive bottom line results.

A.M. Best has a favourable view of Maxseguros' overall profile within the ultimate parent's structure and recognises the benefits gained from this, particularly from the active involvement of EPM senior management.

HIIG's depth of resources will be extremely beneficial to the members and the long-term success of these programmes."

The deal was facilitated by Stonybrook Risk Management, which will act as the financial advisor for mezzanine financing for Energi through Stonybrook Capital.

Allison & Mosby-Scott expand captive offering with VT licence

Allison & Mosby-Scott is now licensed to practice law in Vermont in a move that will help the firm support its clients with captives domiciled in the state.

Michael Scott, attorney at Allison & Mosby-Scott, was sworn into the Vermont Bar on 9 August.

The Allison & Mosby-Scott team have more than 60 years of legal experience and operate in the Central Illinois area.

Founded in 2000, the firm provides clients with a range of captive based services, including captive best practices, feasibility studies and formation assistance, employee benefits, and expert witness services regarding captive best practices.

In a statement announcing the news, the firm said it hoped "being licensed to practice law in the State of Vermont will allow us to better serve our captive insurance company clients, especially those with Vermont captive insurance operations".

NCCIA NEWS

NC Captive Insurance Association

2018 Annual Conference

BLACK MARKET IS THE CANNABIS INDUSTRY'S LARGEST PROBLEM

The largest problem for cannabis is the black market according to Matthew Queen, chief compliance officer and general counsel of venture captive management.

Speaking on a panel discussing whether the cannabis market is an insurable risk at the conference in Charlotte, Queen highlighted that there are some obeying the law and paying their taxes, but "it's obvious that some people are giving in to the temptation".

Karen Landrum, consulting Actuary at Merlinos and Associates, said that theft is huge in the cannabis industry.

She said that "without a [cashless] solution, cash is used a lot", and there "is not a lot of product liability tracking for cannabis in the US".

Commercial property is something else that is a "very important consideration for captive risks" according to Landrum. Workers compensation is also something that could cause an exposure.

Landrum also said that if you are looking to insure your cannabis business, your prices would be based off your exposure.

She explained: "The problem is there are a lot of things you have to consider over prices. For product exposure, everybody Is trying to find out what that would be."

OBLIGATIONS NEED TO BE MET FOR ALTERNATIVE INVESTMENTS

When it comes to alternative investments, you need to meet your obligations, according to Rob Ramos, senior account executive at JLT Insurance management.

Speaking on a panel about investment during the conference, Ramos highlighted that "property is not easy to sell sometimes", and that at the captive level, captive managers need to receive help by clients meeting their obligations.

Ramos said that captive managers are going to "work with you", but "have to put the insurance first and make sure you meet all those obligations".

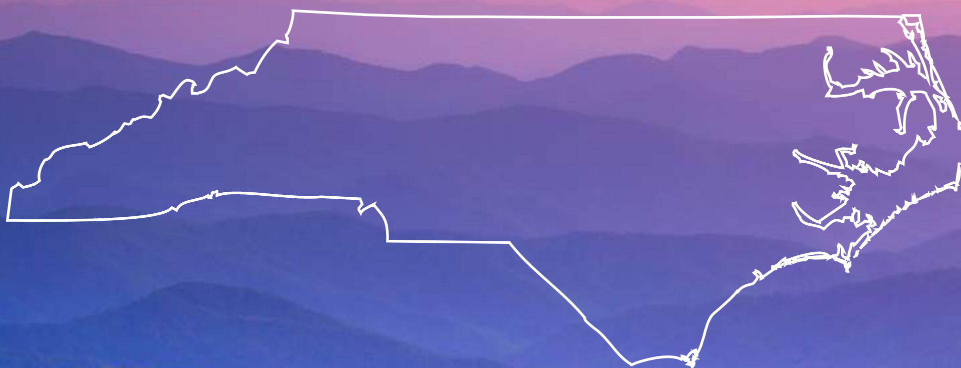
He added that when issuing an alternative investment, communication and transparency is key.

Another panellist, Leane Rafalko, chief captive analyst at the North Carolina Department of Insurance (NCDOI), agreed with Ramos. The moderator, TJ Strickland of Rives & Associates, moved on to discuss life insurance policies, asking Rafalko if the NCDOI does them.

She said although the NCDOI does not do them, "we are aware captive owners may want their captive insurance company to invest in life insurance policies, the department, when vetting the captive insurers investment policy, ensures the criteria for approving these types of investments are included such as the beneficiary and owner of the life insurance policy is the captive insurer".

She added: "The issuing life insurance company must have an 'A+' with A.M. Best and has maintained the rating for at least three years, the issuing life insurance company must guarantee the cash surrender value of the policy, and the cash surrender payment are made to the captive insurer in a timely manner."

Ramos admitted that he personally had not seen a life insurance policy where a captive is a beneficiary, but that he had seen life insurance policies that had been admitted by a captive.



North Carolina:

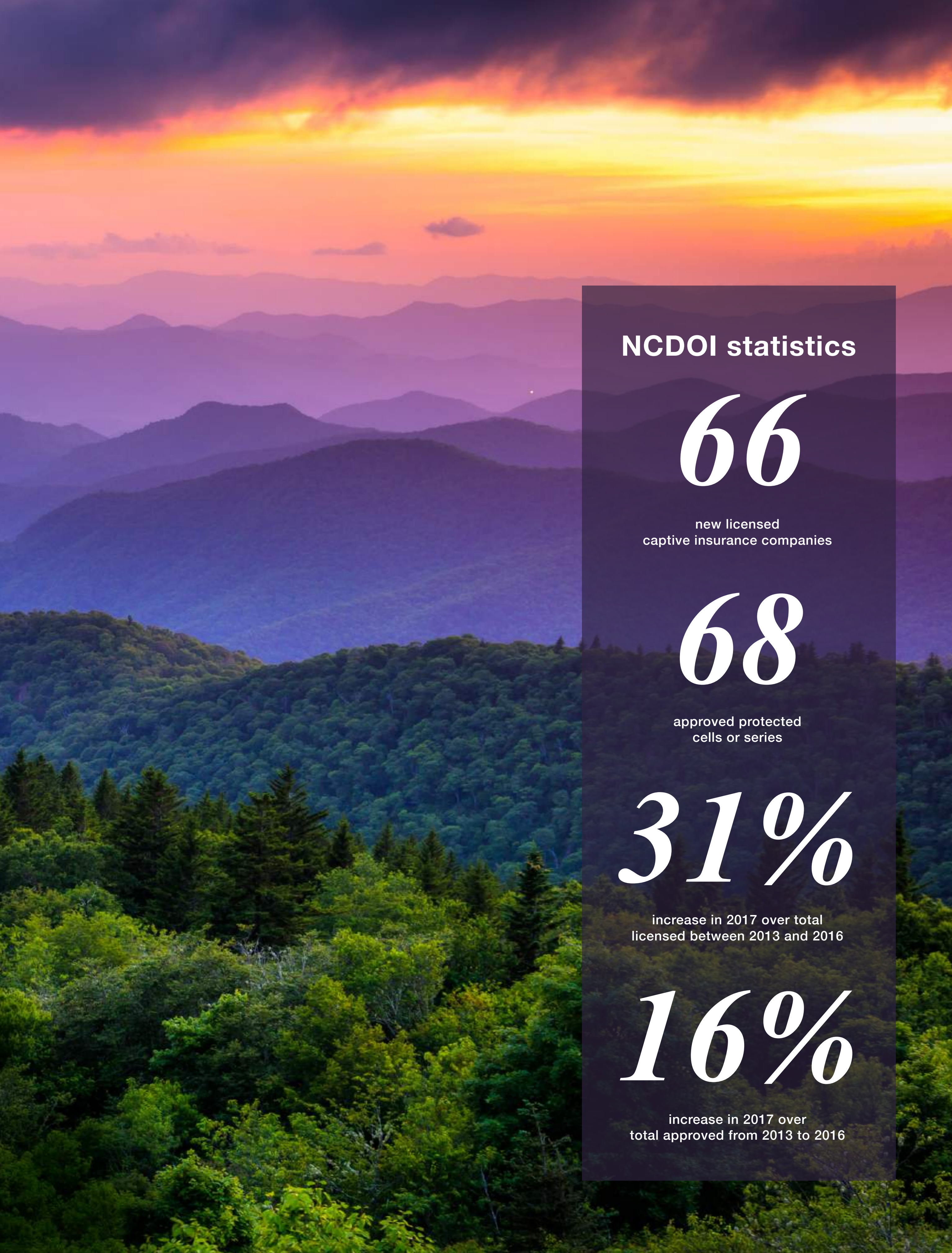
the fastest growing domicile in the west

The NCCIA’s 2018 Annual Conference as Ben Wodecki reports

The North Carolina Captive Insurance Association’s (NCCIA) 2018 Annual Conference saw industry experts from across the state, and the US, descend on the Hotels Sheraton and Le Meridian to expand their knowledge on the fastest growing US captive domicile.

The conference began with an in-depth captive 101 by Debbie Walker, senior deputy commissioner of the North Carolina Department of Insurance (NCDOI), Patrick Long of River Oak Risk, and David Sayles of Berkley Accident and Health.

Officially opening the event, however, was Col. J. Quincy Collins, a retired US Air Force pilot who was captured during the Vietnam War. Collins gave honest and terrifying stories that showed how far the human spirit can be stretched, and how much service personnel could suffer in defense of a nation. Later, Jeremy Colombik, president of Management Services International, Martin Eveleigh, president of Atlas Insurance Management, and Jonathan Reich, of Womble Carlyle Sandridge & Rice received the distinguished service award for their work on the NCCIA board of directors.



NCDOI statistics

66

new licensed
captive insurance companies

68

approved protected
cells or series

31%

increase in 2017 over total
licensed between 2013 and 2016

16%

increase in 2017 over
total approved from 2013 to 2016

The captive insurance industry has added $71 million to North Carolina's economy in the years between 2014 and 2017

Eveleigh commented: "It's nice to have my time working as a board member here recognised."

"I've really enjoyed working on the board, it's been five years and during that time we've seen tremendous growth here in North Carolina, that's been great to see."

During the same session, Morgan Weatherly, senior account manager at Atlas Insurance Management, and Anne Marie Towle, executive vice president and consulting practice leader of JLT Insurance, were appointed to the NCCIA board.

The captive insurance industry has been a boom for North Carolina's economy, and in a later session, Walker showed that the industry had added $71 million to the state's economy between 2014 and 2017.

She highlighted that last year, the NCDOI licensed 66 companies and 68 cells.

Walker said that the NCDOI was "really proud of the growth and that the industry is choosing North Carolina as their domicile".

"We have really grown and that has allowed us to remain responsive and up to date with legislation and regulation."

She highlighted that it has been a full five years since the state's captive programme was passed and that the NCDOI was really happy with the results.

During the conference, speakers and attendees highlighted a range of issues. For example, Mark Elwell, vice president of risk at RMC Group, suggested that tax reform, Internal Revenue Service (IRS) scrutiny, and the paradise papers are key reasons as to why more captives are redomiciling onshore.

Elwell said that "there is still a stigma to being offshore" and that "tax reform can lead to a lot of companies redomiciling".

Self-procurement taxes and previous bad experiences with regulators are other reasons that Elwell highlighted as instances that captives may want to redomicile.

But Elwell pointed out that, ultimately, the captive and client's needs and risks affect the decision, and said there is "nothing wrong" with being an offshore domicile.

In another session, NCDOI senior deputy commissioner Michelle Osborne highlighted that technology is in a period of renaissance and captives have a massive part to play.

Osborne said that the future would see "75 percent of all cars [being] autonomous", and autonomous car manufacturers,

including Waymo and Tesla, are offering insurance products on purchase.

She said: “Things are happening quicker than ever—I call it the renaissance of technology.”

Osborne, who has 25 years’ experience in the property and casualty side of insurance, said that when she was in kindergarten, she had no idea she’d be in the insurance industry, but that “once you’ve been in the industry, it always finds a way to pull you back in”.

Osborne highlighted that there are “more laws that need to be modernised today” to make the industry “honest and right for the consumer”.

“When you can’t find a place to put something, you find a way to insure it, and that is why the captive industry is so amazing.”

Finally, what was arguably one of the most memorable aspects of the conference for all attendees, was the 70s disco.

Here, there were fake afros, vibrant colours, and even a hot dog costume, as attendees let their hair down and enjoyed what was an unforgettable party at an unforgettable conference. **CIT**

Top 5 industries for captive insurance company insureds:

19%

Healthcare

18%

Financial and insurance activities

13%

Construction

8%

Manufacturing

8%

Information technology and communication

North Carolina is ranked the number one domicile in the world for number of captive insurance companies licensed in 2017 for the second year in the row.

Top 5 protected cells/series' insureds by industry:

32%

Healthcare

14%

Wholesale and retail trade

7%

Administrative and support service activities

6%

Construction

6%

Information technology and communication

Power to the workers

Martin Eveleigh, chairman of Atlas, discusses the company's fortunes in 2018 and explains why he expects workers' compensation to continue to be an important market

Ned Holmes reports

How has the first half of 2018 been for Atlas?

Atlas has had a very good first half of the year, perhaps the best ever. We have formed captives writing workers' compensation, general and auto liability, warranty risks, credit risks, motor truck cargo, and a niche healthcare programme.

In the formation process right now, we also have captives writing workers' compensation, compensation, general liability and auto, tenant liability, and accident and health.

We have also seen members added to group captives leading to premium growth.

How strong do you think the captive market is?

From what we are seeing, the captive market is strong.

It's true that there have been a couple of tax cases that went against the taxpayer, but we need to remember that each case depends on its own facts and the fact patterns in those cases may not have been all that good.

It is also worth remembering that other recent cases such as Securitas and Rent-A-Center, which dealt with larger captives, went in favour of the taxpayer.

As far as the soft market is concerned, captives have done well over a number of years during which a soft market has pertained.

Insureds still see advantages in captives that enable them to restructure insurance programmes to make savings, have more control over claims, potentially fund employee benefits and also cover risks on manuscript policy forms.

Looking ahead what do you see impacting the captive market in general over the next 12 months?

It's hard to see anything very significant happening in the next 12 months that will impact the captive market. I do think solutions for cyber liability will mature and that captives will have a growing role to play there. Gradually, captives will start to address risks associated with the blockchain and artificial intelligence, but I emphasise 'gradually'. Then, as we get to the middle of next year, changing economic conditions may well have some effect although probably nothing dramatic.

How has your workers compensation business faired in 2018? What trends have you noticed and what trends do you foresee in the future?

Workers' compensation has been busy for us this year and we expect that to continue. In recent years, smaller employers have been moving away from retro programmes, which gave them potential for back-end savings to guaranteed cost programmes with a high deductible and up-front savings. It makes a lot of sense to finance those deductibles in a captive.

This move to captives is not confined to smaller employers. Larger companies know that rates can't fall forever and that it is prudent to prepare for future rate rises by restructuring now and putting a captive in place. This view is confirmed by carriers we speak to.

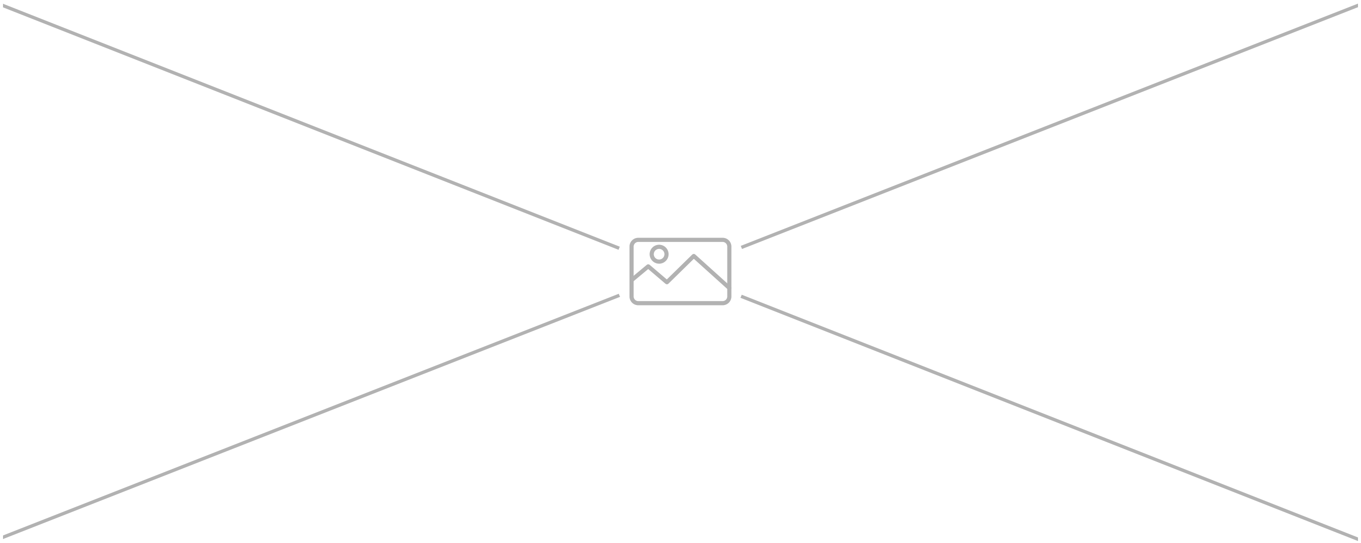
What did you enjoy most about the NCCIA captive conference?

I had a wonderful time at this year's NCCIA conference. While I wasn't able to attend many of the educational sessions, I personally had a lot of worthwhile meetings with other attendees. I particularly enjoyed networking at the 70s disco night reception, which Atlas sponsored. It was fun to see everyone dressed up and having a good time. **CIT**

“Workers' compensation has been busy for us this year and we expect that to continue”

Martin Eveleigh, chairman, Atlas Insurance Management


Industry Opinion
A soft decision with hard ramifications?
Ok



Microsoft's decision to settle with the State of Washington Insurance Commissioner could have interesting implications for the US captive market

Ned Holmes reports

In August, three months after it were issued a cease and desist order, Microsoft's Arizona-based captive, Cypress Insurance, announced it had made a settlement agreement with the State of Washington Office of the Insurance Commissioner.

The decision to settle has only cost Microsoft $876,820—$573,905 in unpaid premium taxes and $302,915 in interest and penalties—but its cost to the captive insurance industry may be much greater.

Control alt desist

The cease and desist order issued by the State of Washington Office of the Insurance in May required the captive to stop transacting insurance without a licence and to pay tax on its written premiums. While Cypress is itself domiciled in Arizona, its sole insureds, Microsoft and its subsidiaries are based in Redmond, Washington.

Insurance companies are required by Washington state law to pay a two percent tax based on their written premiums, a revenue which is sent to the state general fund to pay for a variety of programmes.

According to the Office of the Insurance Commissioner, Cypress didn't hold a certificate of authority to transact insurance in Washington State, didn't hold a Washington state surplus line broker's licence to place non-admitted insurance in the state, nor is insurance coverage provided by the captive placed through a surplus line broker licensed in the state.

Additionally, it claims Cypress has not paid premium tax on the $71,194,935 it collected between 2013 and 2018, representing $1,423,898.70 in unpaid premium tax.

According to the order, Cypress's actions, therefore, violate "Revised Code of Washington (RCW) 48.05.030(1) (certificate of authority required), RCW 48.15.020(1) (solicitation by unauthorized insurer prohibited), RCW 48.17.060(1) (license required), RCW 48.14.020(1) (failing to remit two percent premium tax),and RCW 4S.14.060(l)-(2) (failing to timely remit two percent premium tax)".

Industry outlook

John Dies, managing director of tax controversy at alliantgroup, believes the case is evidence that states are beginning to realise that captive insurance is robust and might generate revenue.

"What they didn't realise is that many of the large corporations, like Microsoft, have captive insurance companies because they have the resources to compete with third-party coverage costs and know their own risks better."

"If Microsoft doesn't like the pricing that they're getting on insurance, they have the resources to give themselves a better price by hiring actuaries. The state of Washington has realised that Microsoft was basically engaged in the insurance industry in the state but without the state's permission."

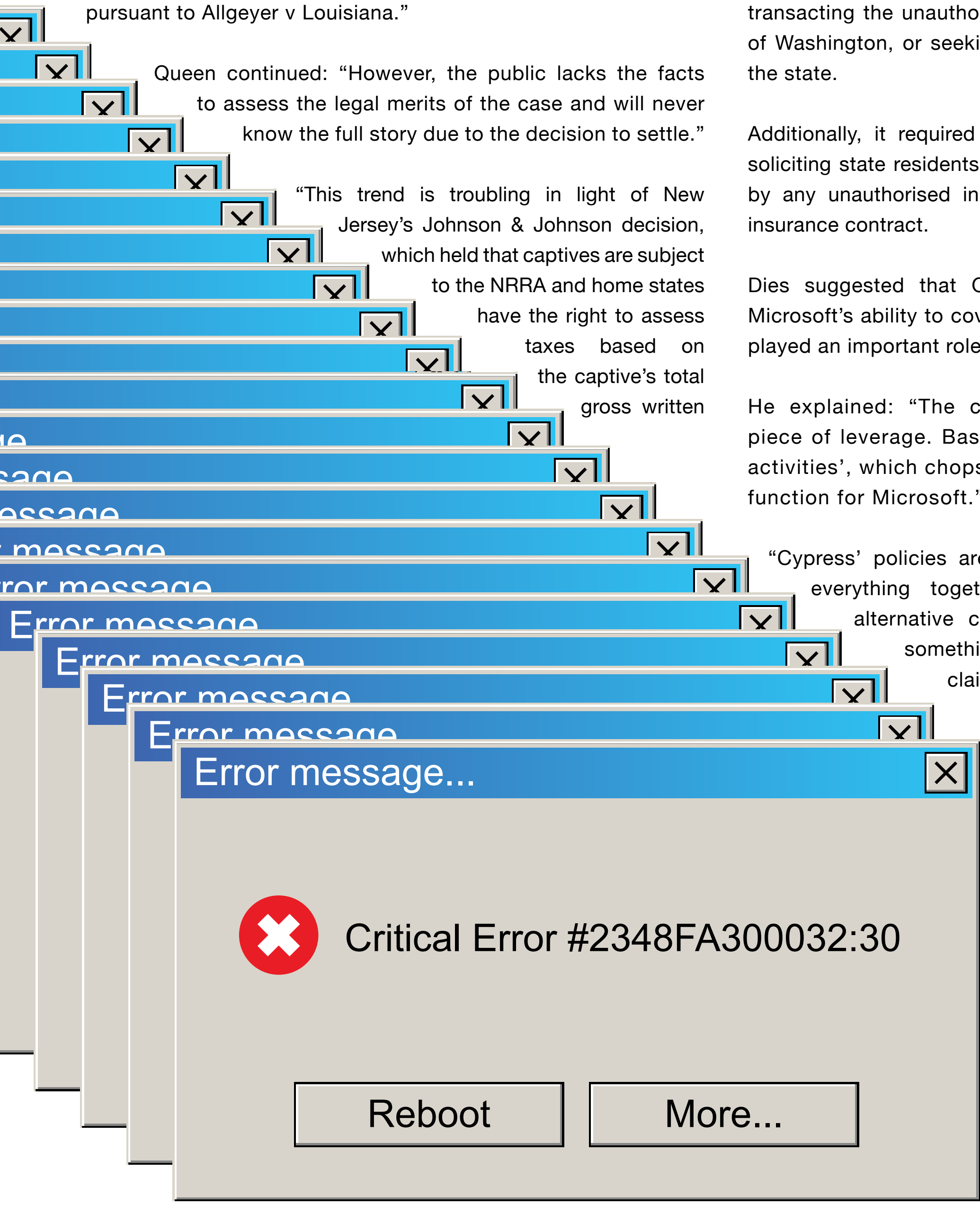
Matthew Queen, chief compliance officer and general counsel at Venture Captive Management, suggested that some of the arguments put forward by the State of Washington Office of the Insurance Commissioner "appear weak".

He expanded: "In particular, Washington's focus on the captive's lack of a surplus lines broker's license or the existence of a surplus lines broker should be irrelevant as Microsoft has the absolute right to purchase insurance from a non-admitted carrier pursuant to Allgeyer v Louisiana."

Queen continued: "However, the public lacks the facts to assess the legal merits of the case and will never know the full story due to the decision to settle."

"This trend is troubling in light of New Jersey's Johnson & Johnson decision, which held that captives are subject to the NRRA and home states have the right to assess taxes based on the captive's total gross written premiums–not just the premiums associated with the taxing state. This is a radical extension of state power that appears to violate the 14th Amendment's Due Process Clause."

"It appears that Washington has taken a similarly aggressive position with respect to its premiums taxes and intends to continue litigation on this front until it's stopped by strong defence counsel."



Footing the Bill

The cease and desist order, Order No.18-0220, issued to Cypress Insurance on 9 May prohibited the captive from engaging in or transacting the unauthorised business of insurance in the state of Washington, or seeking and obtaining insurance business in the state.

Additionally, it required the captive to cease and desist from soliciting state residents to purchase any insurance to be issued by any unauthorised insurer or induce them to purchase any insurance contract.

Dies suggested that Order No.18-0220, and its impact on Microsoft's ability to cover its risks while the case was ongoing, played an important role in the company's decision to settle.

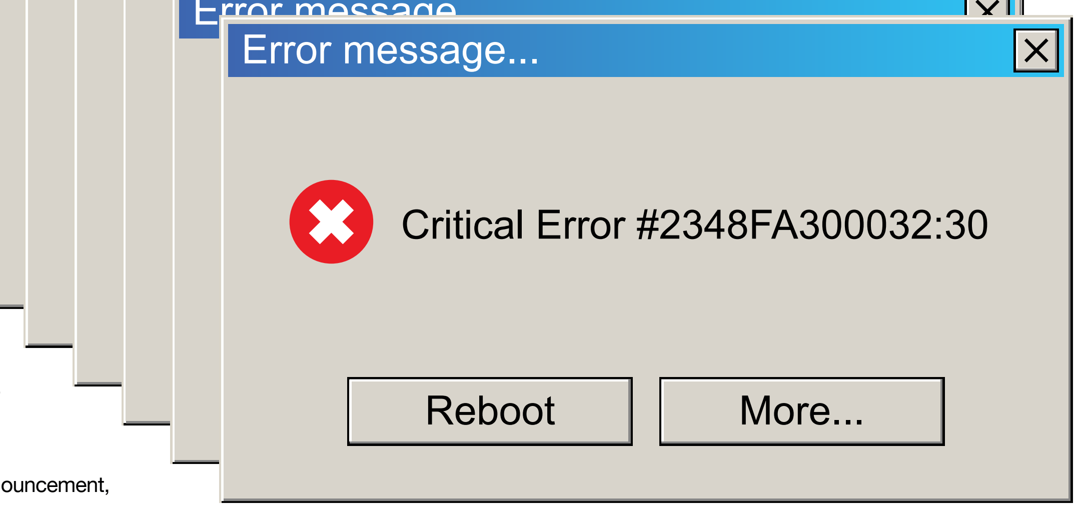
He explained: "The cease and desist order was a huge piece of leverage. Basically, it says 'stop all your insurance activities', which chops off the captive's ability to perform its function for Microsoft."

"Cypress' policies are very complex, so the act of getting everything together, making sure it works, finding alternative coverages and the risk of not having something in place when you do have a serious claim, is huge."

"The cease and desist order was fairly substantial leverage. My assessment of the situation is, the fact that Microsoft was not in a position to immediately comply or put an alternative policy in place forced their hand on the issue."

According to Queen, Microsoft's decision to settle "reflects a reality about the American justice system".

He said: "Justice is available, but it is frequently not worth the time or money. Defence costs and plea deals have reduced the speedy right to trial into the exception to the rule rather than the standard operating procedure.”



Copy and paste? Ramifications for the captive market

Following Microsoft’s settlement announcement, Mike Kreidler, the Washington state insurance commissioner, said he was pleased with the outcome and discussed his plans to turn his attention to more captives–a decision that could have a lasting influence on captives across the US.

He said: “Captives are a grey area in state law and this is the first case where we’ve tested them.”

“I encourage captives insuring risks in Washington—and that want to be proactive in the interest of fairness—to contact my office to start conversations about their portfolios. I want to make sure that all insurers pay their fair share as part of doing business here.”

Dies highlighted this as the biggest takeaway from the case, suggesting that it was a shot across the bows for captives in the state and a warning that they should make themselves known to the Office of the Commissioner or find themselves facing a similar fate to Microsoft.

Perhaps a more pressing issue, however, is whether other states will follow the example set by Washington.

“I don’t see this as an issue that’s going away,” said Dies, “I would expect other states may take this up, particularly when you look at how quickly Microsoft settled this case because of the leverage I mentioned.”

States will be left with a decision to make, on one hand, is the financial gain that stands to be attained from following Washington’s example, however, on the other is the danger that taking such an action will mean they gain a reputation as being unfriendly to captives.

“I guess it’s a revenue decision,” explained Dies. “Whether the revenue they’re losing by allowing insurers to be there without complying is greater than the revenue they will lose when the people say they no longer want to be domiciled there.”

According to Dies, it will not be as easy as just copy and pasting for other states to follow Washington’s footsteps.

He said: “The tricky part for states is going to be determining who is or isn’t complying. It’s not like there are filings that allow you to immediately find out every company and their state that has an active captive insurance company. The Microsoft company is hard to miss, but states are going to have a complex issue on their hands because they’re going to have to figure the economics of the situation with limited data.”

“Maybe the easy answer for all of them is if you’re the big ones, generate some revenue before coming up with a compliance-friendly policy that encourages people to come to you ahead of time, instead of making you chase and catch them to force compliance.”

Loading

While the rest of the US captive market waits for their state to process the situation and make a move, or indeed not make one, on this issue, companies in Washington with captives may be scrambling to ensure their affairs are in order.

JLT Insurance Management released a statement shortly after the settlement decision, advising “all clients who have parent companies with headquarters or operating units in Washington to consult with their tax professionals to determine their next steps if any”.

Dies has predicted that companies in Washington will be considering what their plan of action would be if they were the Commissioner’s next target.

He said: “At a large company in Washington right now, they will be looking to see what their plan B0 looks like if they get a cease and desist order, how quickly they can put something else in place and/or should they go ahead and move in that direction right now to avoid this all together and solve the problem before Washington raises this issue.”

Another question facing captives is whether the commissioner will retrospectively target companies that are no longer based in the state.

Dies commented: “Suppose they move their insurance carrier, suppose they get into compliance without being licensed in Washington, does the Office of the Commissioner still come after them for the years they had their unlicensed insurance with them? That just depends on the appetite of the commissioner, which is obviously, compared to other states, much more aggressive so far.” **CIT**

Emerging Talent

Showcasing the new generation of captive professionals

Michael Arcangel, senior captive financial analyst, NCDOI

Personal bio

I grew up in Wake Forest, North Carolina, and currently enjoy living in Raleigh, North Carolina, with my wife and two dogs. When I'm not busy regulating captive insurance companies, you can find me mountain biking, woodworking, volunteering, or binging Netflix.

Professional profile

I graduated from the University of North Carolina at Wilmington with a bachelor's degree in Business Administration with a concentration in Accounting in 2012. Over the last two years, I have worked with the Captive Insurance Companies Division of the North Carolina Department of Insurance (NCDOI).

Prior to my work with the NCDOI, I was an auditor for the state's alcohol beverage control commission for four years. I am currently pursuing my Associate in Captive Insurance designation.

What has been your highlight in the captive industry so far?

I enjoy travelling to conferences to network and to learn from more experienced individuals. I think one of the great things about the industry is that it is expanding, yet small enough where personal connections can be formed and maintained.

What/who have been your influences in the captive industry?

Mostly the leadership of senior deputy commissioner Debbie Walker and all my coworkers with significant insurance and regulatory experience. They have helped me form the perfect blend between being a partner with the industry and my duty as a regulator.

What is your impression of the industry?

My impression is that it is an innovative industry where creative ideas are used to benefit companies' risk management needs and the industry will continue to be adaptive to those needs. I also think a little more diversity in the industry would be beneficial.

What advice do you have for someone considering a role in the industry?

I am forever grateful I fell into this industry and hope to have a long career in captive insurance. Regulators get an overview of every aspect of the industry and interact with all the service providers needed to manage captive insurance companies. From my view point, I would recommend anyone to consider any role within the industry.

> The NCDOI is very fortunate to have Michael Arcangel as a member of its captive insurance regulatory team.
>
> It is hard to believe that Arcangel has only been with the department for two short years. He has made the most of that time, already receiving a promotion to senior financial analyst. Arcangel brings fresh ideas to the projects on which we are working, and he is also analytical, detail-oriented, logical, and technologically savvy.

Debbie Walker, senior deputy commissioner,
North Carolina Department of Insurance

Michael Arcangel

Cutting-edge risk

John Huff, CEO of the Association of Bermuda Insurers and Reinsurers, explains that Bermuda is leading the defence against cyber risk and why the International Cyber Risk Management Conference is an important asset in that fight

Ned Holmes reports

Cyber risk is quickly evolving into one of the most dangerous challenges that businesses face, as global connectivity grows and the attack surface widens.

The 'cybercrime epidemic' is, according to the Cybersecurity Ventures 2017 Crime Report, the greatest threat to every company globally and could cost the world $6 trillion annually by 2021. The insurance market is evolving to help companies protect against the threat and Aon Insight suggests that cyber insurance premiums will experience the most rapid growth of any insurance product premiums by 2021.

As a world leader in insurance, Bermuda and it's global insurance market is not shying away from that challenge and between the 6 and 7 of December this year, the island will bring together some of the industry leaders on cyber risk for the International Cyber Risk Management Conference (ICRMC).

Captive Insurance Times spoke to John Huff, CEO of the Association of Bermuda Insurers and Reinsurers and a speaker at the conference, about cyber risk and the conference itself.

Have you seen a growth in the relevance of cyber risk since you took your current role at the association?

Absolutely. I just started as CEO of the Association of Bermuda Insurers and Reinsurers in January of this year. I previously served as a state insurance regulator in Missouri, and was president of the US National Association of Insurance Commissioners. Cyber risk is fast becoming one of the most complex and challenging situations for individuals and businesses worldwide and Bermuda's global insurance market is leading the way.

What current and emerging cyber risk trends have you identified in 2018?

Enterprises of all sizes are assessing their appetite for retaining cyber risk. It's not just the large organisations. Likewise, insurers and reinsurers are assessing where they want to be in taking on cyber risk, including taking stock of any 'silent' cyber exposures and stress testing these scenarios.

Insurers are really stepping up to add value when policyholders are facing network security and data privacy events. Building and immediately deploying a network of reliable partners to respond quickly and efficiently to events can be crucial to containing losses and preserving reputations.

New privacy protection laws are adding additional complexities and require sophisticated coverages.

How are cyber-insurance services and offerings addressing them?

Managing cyber risk is not just about risk transfer. The insurance underwriting process alone contributes to raising awareness of cyber risks. Insurers are scrutinising risks and the underwriters are rewarding increased levels of cyber security.

New coverages are being developed for regulatory actions and to fill gaps identified in traditional property and liability coverages.

How much of a role do you think captives can play in helping cover cyber risk?

Insurance coverage for cyber risk is evolving and risk professionals are exploring all kinds of structures. Captives may be a tool to fill any coverage gaps or viewed as supplemental to commercial coverage.

For example, businesses may decide their appetite for risk allows them to take a primary layer of coverage through a captive and get peace of mind with excess layers in the commercial market.

What opportunities does the conference offer for captive/risk professionals?

The ICRMC is an essential forum for risk professionals with an agenda that focuses on risk transfer approaches to cyber risk management. Bermuda's global insurance market includes some of the leading cyber insurance carriers and professionals.

What are you most looking forward to about the conference?

Besides being in Bermuda in December and the wicked art collection at the Hamilton Princess? Seriously, there are some cutting-edge industry leaders coming together for this conference and it promises to be a great exchange of ideas on managing cyber risk. **CIT**

> "Cyber risk is fast becoming one of the most complex and challenging situations for individuals and businesses worldwide and Bermuda's global insurance market is leading the way"

John Huff, CEO, Association of Bermuda Insurers and Reinsurers

Captive industry dates for your diary

NRRA Conference Chicago	Guernsey Insurance Forum Guernsey
October 03-05 riskretention.org	October 11 weareguernsey.com
Hawaii Captive Insurance Council Annual Forum Hawaii	**Captive Insurance Council of DC Annual Conference** Washington, DC
October 15-18 hawaiicaptives.com	October 24-25 dccaptives.org

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Comings and goings at SRS and the LMA

Strategic Risk Solutions (SRS) has hired Dana Williams as the firm expands its presence into North Carolina.

Williams has been appointed as regional manager for North Carolina and Ohio and will be based in SRS's new office in Charlotte, which is the firm's first permanent presence in North Carolina.

Williams, who brings more than 15 years of experience in senior finance positions in the insurance industry, most recently held the role of CFO of Hub International Eastern Canada and Worldwide Broker Network.

Prior to her role at Hub International, Williams was COO at Steadfast as well as spending several years in the Cayman Islands' captive industry.

Williams said she admired what SRS had achieved and was excited for a new challenge in her career.

She commented: "This opportunity allows me to return to the captive insurance industry and be more actively involved in day to day financial management as well as working with a variety of client organisations."

"North Carolina is a rising, progressive domicile and I am looking forward to working with the regulators and local captive community."

SRS president Brady Young said the firm believes the addition of Williams to the North Carolina office will help it better serve their clients there.

Young stated: "We have worked with Dana Williams on a couple of different projects including our expansion into Barbados and are very pleased to be able to welcome her full-time to SRS."

"Her experience as a financial executive in the insurance industry is exceptional and we are confident she will be a valuable addition to the firm especially in expanding our presence in North Carolina and growing that presence in Ohio."

"We are keen to do more work in these domiciles."

Sheila Cameron will be the next Lloyd's Market Association (LMA) CEO, succeeding David Gittings, who is stepping down at the end of the year after 12 years in the role.

Cameron is currently head of international operations at Navigators Underwriting, where she is responsible for leading all operational and change management activity within Navigators International, which includes its Lloyd's business together with its global platforms in Europe, Asia, and Latin America.

She is also chairman of the LMA Operations Committee and a member of the Target Operating Model Board.

Prior to her role at Navigators, Sheila was director of group operations at Hiscox and served in a number of roles at Xchanging, including COO of the claims business.

Cameron said she is honoured and excited to lead the LMA and plans to build on the "immense work" done by Gittings.

She commented: "The LMA plays a crucial role in making the market a better place for all its participants."

"I look forward to working together with Lloyd's on the evolution of its strategy, a renewed focus on our customers and the delivery of market modernisation."

Neil Maidment, LMA chairman, said the board look forward to working with Cameron.

Maidment said: "Sheila Cameron's background and experience in the London market will be invaluable in driving the LMA's agenda forward."

"David Gittings has worked successfully over many years to ensure that the interests of market firms have been effectively represented and we will be sorry to see him go."

"I would like to take this opportunity to thank him on behalf of our members for all he has achieved." **CIT**