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ISSUE111
23.11.2016 WEDNESDAY
captiveinsurancetimes.com

‘Perplexing’ micro captive notice attracts criticism

The Self-Insurance Institute of America (SIIA) has asked the Internal Revenue Service (IRS) to grant more time to 831(b) captives that need to comply with Notice 2016-66.

SIIA’s letter, sent to the IRS on 17 November, was issued in response to the IRS and the US Treasury’s 1 November Notice 2016-66, which formally labelled micro captive transactions as “transactions of interest”.

The notice requires reporting by any taxpayer involved in micro captive transactions over a number of past years in which the open statutes of limitations applies.

The filing deadline for this is 30 January 2017, 90 days from the date of issuance.

Ryan Work, vice president of government relations of SIIA, said: “Considering the large amount of reportable information being requested, the amount of past years under potential review, and the lack of guidance on the soon to be enacted Protecting Americans from Tax Hikes (PATH) Act requirements, we believe an extension is necessary.”

The letter suggested that “extending the comment deadline for at least 90 days after the compliance deadline is more than reasonable and should be harmless”.

The letter explained that even captives abiding by the rules could face unnecessary fines and punishment because they are unable to compile the information requested in “such a short time span”.

Most captives affected by the notice will “likely have at least one insured business and one shareholder that also reports, and may have dozens of each”, according to Work.

The letter stated: “The total number of taxpayers required to file reportable transaction forms will easily exceed tens of thousands, posing difficulty for both the industry in compiling the data, and the IRS in reviewing.”

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‘Perplexing’ micro captive notice attracts criticism

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“We imagine this would also create a burden on the IRS,” the letter added.

According to Work, the fact remains that the notice, outside of being effective immediately with just 90 days to report, throws out a broad net to nearly all captives, regardless of whether they exhibit potentially abusive practices or not.

Work said: “Approaching this complex issue requires more detailed and carefully crafted guidance, much like the issues already faced by the industry with many of the PATH requirements.”

Tim Tarter, a captive audit defence expert, suggested that the timing of the IRS and Treasury’s notice on micro captive insurance arrangements is “perplexing”.

Tarter said: “What government interest is being served by the release of the notice now, only a few months before the US Tax Court releases its opinion in Avrahami?”

Abusive micro captive transactions previously appeared on the IRS’s ‘Dirty Dozen’ list, which calls out tax scams that the IRS will be targeting in the coming year.

“It is certainly no secret the IRS is examining many taxpayers involved in micro captive insurance transactions,” Tarter said.

When the Dirty Dozen list was released, IRS commissioner John Koskinen said: “Taxpayers should steer clear of unscrupulous promoters who sell phony tax shelters with no real purpose other than to avoid paying what is owed.”

He explained: “These schemes can end up costing taxpayers more in back taxes, penalties and interest than they saved in the first place.”

According to Tarter, the notice means that the IRS and Treasury have made a determination that at least some of these transactions have a potential for tax avoidance or evasion.

So-called transactions of interest were first established by the IRS in 2006 and since then, only six have been labelled as such, including micro captive transactions.

Tarter explained what the notice means in practice: “The notice alerts persons and entities involved in micro captive transactions, and their material advisors, to various disclosure responsibilities and the penalties that arise from failure to fulfil them.”

The notice generally defines micro captives as transactions of interest if one or both of the following apply: the captive’s insured losses and claim expenses are less than 70 percent of its earned premiums; or the captive has made financing, for example, guarantees, loans or capital, available to its insured or related persons.

Tarter suggested that since the notice “fails to provide any definitive guidance” as to what micro captive entities will survive Tax Court scrutiny, “it is unlikely to deter most informed micro-captive participants from moving forward with their planned captive transactions”.

He said that all informed business owners “should already be aware of IRS scrutiny in this arena and will not be dissuaded by the additional reporting requirements demanded in the notice”.

He concluded: “The Treasury and the IRS are currently soliciting comments on how micro captive transactions might be addressed in future published guidance. Perhaps they should simply await an opinion from the Tax Court.”

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CapAlt offers captive services to MediGroup

Captive Alternatives (CapAlt) has entered into a sponsorship agreement with MediGroup Physician Services to provide captive start-up services to its members.

Using its protected captive model, CapAlt will provide set-up and administration services to eligible MediGroup members, as well as MediGroup member organisations.

Andy Klearman, CEO of MediGroup, said: "With the growing popularity of captives, MediGroup has determined that it should include the offering of a captive programme as part of its mission to provide leadership and education to its members."

Mark Jacobs, CEO of CapAlt, added: "We anticipate that the ability to establish a protected captive quickly is going to be very beneficial for MediGroup members and look forward to working with MediGroup Physician Services to extend the benefits of a protected captive to their members and related associations."

Fox Rothschild wins reg approval for New Jersey captive

The State of New Jersey's department of banking and insurance has given Fox Rothschild the approval for an onshore captive insurance company to insure underground storage tanks.

Carl Anthony Maio and Sandra Romaszewski, partners of Fox Rothschild, led the team in securing a captive certificate for Founders Indemnity Group.

The captive is now licensed to write insurance policies for underground storage tank owners in New Jersey in the areas of liability insurance and property and casualty insurance.

According to Fox Rothschild, recent statistics show that more than 3,000 onshore captive insurers were operating in the US as of 2015. New Jersey ranked 18th on the list with 22 captives licensed.

New group captive for Artex

Artex has launched a new heterogeneous group captive, Command, domiciled in the Cayman Islands.

The captive will cover lines such as auto liability, general liability and workers' compensation.

Artex employees will manage the captive's programme with support from various third-party providers.

Chad Kunkel, executive vice president for group captives at Artex, commented: "As we continue to grow our existing group captives, we found a need to launch a new group captive to meet the needs of the marketplace and our broker partners."

He added: "This programme has excellent coverages, services and pricing that will satisfy the needs of insureds."

"These companies are looking to have premiums based on their own experience, the ability to receive return of underwriting profit, and services to reduce claims as well as an opportunity to have better control over claims."

Stable outlook for J.P. Morgan captive

A.M. Best has affirmed the financial strength rating of "A (Excellent)" and the long-term issuer credit rating of "a" of Park Assurance Company, the single parent captive of J.P. Morgan Chase & Co.

The ratings affirmations reflect the captive's "excellent" risk-adjusted capitalisation, operating performance, liquidity position, risk management strategy, and practices and investment strategy, according to A.M. Best.

The rating agency suggested that, as a single-parent captive, Park Assurance provides J.P. Morgan Chase with "very high" insurance limits and insures some properties with "substantial" insured values.

Coverage lines of the captive include terrorism, workers' compensation, auto liability and general liability.

A.M. Best noted that these coverages are "key components" of J.P. Morgan Chase's risk management strategy, and that Park Assurance benefits from the group's "significant" financial resources.

J.P. Morgan Chase also benefits from the group's risk mitigation and safety programmes.

A.M. Best said: "As Park reinsures a large portion of its global property programme, its exposure to underwriting losses is minimal, barring significant losses from terrorism."

Park also remains dependent on the protection of the Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) of 2015.

While the TRIPRA programme offers significant protection from terrorism losses, A.M. Best suggested that the net impact on Park "could still be burdensome".

A.M. Best added: "Park Assurance's enterprise risk management practices as strong given its close alignment with its parent and the positive impact J.P. Morgan Chase has on Park Assurance's corporate risk culture and its ability to measure, manage and mitigate risk in a prudent and optimal manner."

"Other factors considered in the rating process include, but are not limited to, the diversification in line of business and geography and the explicit and implied support and commitment of its parent."

Argo Group acquires Ariel Re

Argo Group has acquired Ariel Re, an underwriter of insurance and reinsurance business, for around $235 million.

The transaction is expected to close during Q1 2017, subject to regulatory approval.

The acquisition will add new capabilities to the company, including Ariel Re's modelling and risk analysis tool, which will enhance Argo's underwriting analytics.

Heading up the combined business will be Jose Hernandez, head of Argo Group's international business.

Mark Watson, CEO of Argo Group, commented: "Ariel Re is a terrific fit for Argo Group—operationally and culturally. This transaction enables us to build upon the successes realised individually by Argo Group and Ariel Re, utilising our combined strength to deploy capital in selected areas to produce maximum return and continued growth."

"This acquisition is part of Argo Group's strategic initiative to build scale in its London- and Bermuda-based platforms by adding complementary lines of specialty business. After the acquisition, Argo Group will have a well-balanced portfolio mix of approximately 88 percent insurance and 12 percent reinsurance."

S&P Global Ratings has revealed that Argo Group's long-term and financial strength ratings will not be affected by the acquisition.

The rating agency said: "We believe the acquisition's size is relatively small on a net basis. While financial leverage ... will increase to around 26 percent, we expect prospective capitalisation to remain very strong."

Argo Group's financial adviser for the transaction was Aon Securities, while Willkie Farr & Gallagher LLP was its legal counsel.

As part of the transaction, Skadden advised Banco BTG Pactual, part owners of the Ariel Re with Abu Dhabi Investment Council.

Negative outlook for China Railway captive, says Moody's

The China Railway Captive Insurance Company has received an "A2" financial strength rating with a negative outlook from Moody's Investors Service.

This is the first time Moody's has assigned ratings to the China Railway Captive Insurance Company, a wholly-owned subsidiary of China Railway Corporation (CRC).

The ratings reflect Moody's view that the China Railway Insurance Company credit profile is closely aligned to CRC's, as well as its assessment of high-level support from CRC because of its captive status.

According to Moody's, it anticipates that the parent company will provide "operational and timely capital support" for China Railway Captive Insurance's business growth.

Moody's suggested that a ratings upgrade is unlikely, "given the negative outlook", as well as the company's "limited operating track record".

Given that the credit profile of China Railway Captive Insurance is "highly correlated" with that of its parent, Moody's said it would consider upgrading its rating "if the credit profile of CRC improves significantly".

Alternative capital and ILS markets continue to expand

The input of alternative capital into the global reinsurance market is continuing to increase, bringing it closer to a convergence in which traditional providers will become conduits to the capital markets, according to a panellist at the Bermuda Reinsurance Conference.

Attendees at the conference, hosted by ILS Bermuda, heard that the expansion of the market has come from insurance-linked securitisation such as catastrophe bonds.

Panellists, however, explained that this convergence is still in its early stages.

Michael Millette, managing partner at Hudson Structured Capital Management, commented: "We're just starting to see securitisation change the underlying industry."

Millette explained that although the catastrophe bond market has reached roughly $25 billion outstanding, it can "take a long time for other asset classes to gestate".

Speakers revealed that, with the increase in alternative capital over the last few years, the market has now reached a value of $75 billion, with many funds now using collateralised reinsurance.

Dirk Lohmann, chairman and managing partner at Secquaero Advisors, said: "There's a lot of potential for securitisation to optimise insurance companies' capital structures."

The Chelsea Group completes deal for Security Exchange

The Chelsea Group has purchased Security Exchange, a security risk management company. Security Exchange will become a division of The Chelsea Group, providing specialist insurance risk management consultancy services to clients.

Rupert Reid, managing director of Security Exchange said: "The acquisition ... brings our clients significant benefits, as being part of an established group enables us to deepen and broaden our special risks product offering, and provides us with a truly global footprint."

Lord Richard Westbury, chairman of The Chelsea Group, added: "We welcome Security Exchange into The Chelsea Group, at a time when the increasing number and complexity of risks facing organisations, and therefore the need for proven security solutions, has never been greater."

Berkley and ProSential launch team up to launch stop-loss group captive

Berkley Accident and Health has teamed up with ProSential Group to launch ProSential Cap, a stop-loss group captive.
From January 2017, ProSential Group's brokerage firms will gain access the to firm's captive, giving clients the opportunity to benefit from good health risk management.

ProSential Cap will allow small to mid-size companies to replicate the size and stability of a large employer's health plan.

The captive reinsures stop-loss policies of multiple employers to create a more balanced risk profile compared to that of a single employer.

Dean Rowe, vice president of carrier relations at ProSential Group, commented: "Stop-loss group captives have become an important risk-management tool for small and mid-size companies. This agreement gives our brokers a group captive solution developed specifically for their clients and supported by Berkley Accident and Health."

Christopher Brown, president and CEO at Berkley Accident and Health, added: "We are excited about our agreement with ProSential Group. The scale and quality of its network, combined with its health risk management capabilities, creates tremendous opportunity for its clients to benefit from this solution."

Hurricane Matthew to cost US and Caribbean $15 billion

Last month's Hurricane Matthew could cost the US and Caribbean combined economic losses of approximately $15 billion, according to Aon Benfield's Impact Forecasting team.

Impact Forecasting's monthly catastrophe report revealed that US total economic losses could hit $10 billion, while private insurance could see economic losses of up to $5 billion.

Hurricane Matthew also ripped through the Caribbean, causing $2.6 billion of economic losses in Cuba, $1.9 billion in Haiti and $600 million in the Bahamas.

Flooding and strong winds also affected part of Atlantic Canada, where damages and expenses are expected to hit tens of millions of dollars.

Steve Bowen, director and meteorologist at Impact Forecasting, said: "The extensive footprint of Hurricane Matthew left considerable damage and humanitarian impacts from the Caribbean to Canada."

Captives at the forefront of insurance in Asia, says Guernsey

Captives are going to be at the "forefront of innovation in Asia's insurance market", according to Guernsey Finance representatives speaking at its insurance master class event in Hong Kong.

The event, which took place on 8 November, was attended by more than 50 delegates, including insurance and risk managers, family office manages, HR directors, finance directors, lawyers and accountants.

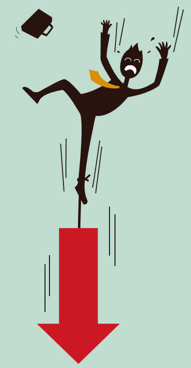
Kate Clouston, director of international business development at Guernsey Finance, said: "Captives allow for improved risk management and a greater understanding of the cost of risk."

"Not only that, but they also provide direct access to the wholesale reinsurance market and great control of claims and result in less reliance on the commercial insurance market," Clouston explained.

She added: "Captives are certainly going to be at the forefront of innovation in Asia's insurance market, and Guernsey is proud to be recognised as a centre of excellent in this area."

Earlier this year, Guernsey representatives signed agreements with both the China Captive Alliance and the Kashgar government to promote captive insurance in the region.

The agreements intend to facilitate business development initiatives between the parties and enable captive insurance market development and information sharing.



Evergreen Insurance ratings downgraded

A.M. Best has downgraded the financial strength rating of Evergreen Insurance Company (EICL), located in Bermuda from "A (Excellent)" to "A- (Excellent)".

The long-term issuer credit rating also dropped from "a" to "a-", however, the outlook of the credit rating remains stable, A.M. Best said.

EICL is a pure captive of the Evergreen Group and is the group's risk management platform.

It underwrites risks in marine, aviation, property, engineering, motor and other liability in relation to group operations.

The ratings downgrade reflects the reduced risk-adjusted capitalisation due to a dividend payment made in 2016, which exceeded the total net income it generated over the past three fiscal years.

According to A.M. Best, negative rating action could happen if "EICL's absolute capitalisation declines materially or if its risk-adjusted capitalisation further decreases sharply".

Greenlight Reinsurance suffers rating drop after run of poor results

Greenlight Reinsurance has had its financial strength rating reduced due to a poor run of underwriting results.

The specialist property and casualty reinsurer works with captives and risk retention groups.

It did report underwriting income of $600,000 in Q3 2016, up from a loss of $31.7 million, year over year.

Aon offers protection against GDPR

Aon has released a new solution to help organisations prepare for implementation of the EU's General Data Protection Regulation (GDPR).

The GDPR, which is set to come into force in the EU in May 2018, will introduce major changes to European data protection law, including stronger enforcement powers and higher fines, with potential liability set at up to 4 percent of global turnover

Aon's new solution, EU Data Protect, will help to protect against some of the potential financial impacts of the regulation.

EU Data Protect includes a GDPR readiness assessment tool that will assist organisations with identifying, prioritising and remediating gaps in their compliance programmes, as well as a cyber impact analysis that employs sophisticated modelling of the financial impact from data breaches under GDPR.

Further functionality includes an EU GDPR insurance endorsement that acknowledges the regulation in a qualifying cyber policy, and access to specialist post-event advisory services.

"The GDPR represents a significant regulatory challenge facing firms that do business in the EU," explained Renette Pretorius, cyber practice leader at Aon's Global Broking Centre in London.

"Its mission is to give citizens back the control of their personal data and equip regulators with sufficient enforcement powers to address the evolving digital landscape and tougher privacy challenges—a change heavily felt across many companies. All businesses operating in the EU, no matter where they are located, should prepare for the impact of this regulation."

But the rise did not stop A.M. Best lowering the Cayman Islands-based reinsurer's financial strength rating from "A (Excellent)" to "A- (Excellent)".

A.M. Best also lowered Greenlight Re's long-term issuer credit rating from "a" to "a-".

The rating agency explained: "The rating actions reflect Greenlight Re's less favourable underwriting results in recent years, including results through 30 June 2016, which have fallen short of A.M. Best's long-term expectations."

"While the company has taken actions to remediate the problematic contracts, it is showing an underwriting loss that under performs most peers on its five-year trend through 2015."

"While A.M. Best acknowledges that the underwriting process and controls have since been strengthened, the current market environment will continue to present challenges and will ultimately test the sufficiency of the current underwriting rigour and enterprise risk management."

Bart Hedges, CEO of Greenlight Re, said in a statement: "We have experienced several years of adverse development on construction defect contracts, which have negatively affected financial year results. We have novated these contracts to limit further exposure to this business. The remainder of our underwriting portfolio continues to perform in line with our expectations."

Ninth Circuit upholds LRRA preemption

The US Court of Appeals for the Ninth Circuit has upheld the federal Liability Risk Retention Act (LRRA) preemption status, in Attorneys Liability Protection Society (ALPS) v Ingaldson Fitzgerald.

The National Risk Retention Association (NRRA) had previously filed its amicus curiae brief in the case before the Ninth Circuit.

In the appeal, the Ninth Circuit held that Alaska Statute 21.96.100(d)'s prohibition on reimbursements of fees and costs incurred by an insurer defending a non-covered claim was preempted by the LRRA.

The Ninth Circuit decided that the Alaska statute placed a restriction on Alaska contracts that was not contemplated by the LRRA, and that was not precluded by all other states. The Ninth Circuit further determined that no exception applied to save the Alaska law from preemption.

An en banc rehearing request is being considered. NRRA executive director Joe Deems commented: "This will be a major victory if the Ninth Circuit upholds its own opinion."

R&Q agrees run-off arrangement

Randall & Quilter Investment Holdings has agreed an arrangement with the Law Society of Ireland in respect of the run-off obligations of the Solicitors Mutual Defence Fund (SMDF).

SMDF provides professional indemnity protection for solicitors based in Ireland.

Ken Randall, chairman and CEO of R&Q Investment Holdings, said: "We are pleased to announce the arrangement with the Law Society of Ireland further demonstrating R&Q's ability to offer finality solutions in a range of different situations."

R&Q Malta also reached an agreement with SIMIA, a mutual insurance company, in September, to provide loss portfolio reinsurance coverage for all insurance contracts previously underwritten by the company.

In the same month, the company also agreed a portfolio transfer agreement of a run-off business from Aviabel.

Pizza captive delivery for Vermont

Vermont has licensed five pure captives and one risk retention group (RRG) since July this year, according to David Provost, deputy commissioner of the captive insurance division at Vermont's Department of Financial Regulation.

The captives included Idem Indemnity Inc, the captive of Brady Corporation; Global Risk Management Services, the captive of Sunex/Liquid Combustion Technologies; Sleep Insurance, the captive of Tempur Sealy International; Mainland VT Insurance Company, the captive of Beacon Capital Strategic Partners; and finally Northeast Casualty Insurance Company, the captive of Clean Harbors.

In addition, Vermont welcomed Hospitality Risk Retention Group, the RRG of Domino's Pizza.

The six new licences bring the total number of captives domiciled to 1077, with approximately 590 active companies.

Provost commented: "We have an active pipeline of companies in various stages of the licensing process, from the initial discussion to filed applications."

"As of 4 November, we have eight applications in process," he added.

This year marked the 35th anniversary of Vermont's captive insurance legislation being signed into law.

Japanese captives remain underutilised, says A.M. Best

With Japan having one of the largest commercial insurance markets in the world, its captive insurance industry remains underutilised, according to an A.M. Best briefing.

The briefing, Growing Role of Japanese Captives, explained that the low utilisation in Japan is partially due to historically strong relationships with major domestic insurance groups, which have traditionally been the largest shareholders of industrial organisations.

According to the briefing, these relationships have evolved in recent years, as evidenced by the continuous reduction in business-related stock holdings by major Japanese groups.

A.M. Best said the decline would suggest that there might be additional Japanese captives in the future.

This growth would be particularly timely as various companies are investing in or starting new subsidiaries outside of Japan, said the rating agency.

In terms of domiciles, Bermuda and Hawaii remain the most popular choices for Japanese captives.

However, domiciles in the Asia-Pacific region, such as Micronesia, have been an attractive choice.

A.M. Best explained that rated Japanese captives currently face an increasing challenge due to the weakening credit profiles of their parent companies.

The rating agency said: "Although parent profile is not a sole factor in assessing the creditworthiness of the captive, this factor is increasingly putting downward pressure on the ratings of captives given their main purpose of managing the risks of captive owners."

"Another challenge for the Japanese captives has been the inclusion of new lines of business associated with the parent's business expansion."

A.M. Best noted that senior management would need further education about the risks and benefits that a captive can provide.

NORCAL buys Preferred Physicians Medical RRG

NORCAL Mutual Insurance Company has acquired PPM Services, the holding company for Preferred Physicians Medical Risk Retention Group (PPM).

As part of the transaction PPM Services, located in Overland Park, Kansas, will partner with NORCAL, expanding PPM's presence in the Midwest.

Steven Sanford, president and CEO of PPM, said: "We are very pleased to be joining such a well-respected company as NORCAL, who shares our commitment to always putting the best interests of physician policyholders first."

"PPM will now be able to leverage the considerable resources of NORCAL to further expand our anaesthesia brand, better respond to changes in the health care environment and deliver additional value to our policyholders."

Scott Diener, president and CEO of NORCAL, added: "This is a great partnership for both companies and an opportunity for NORCAL to continue our national expansion and establish a strong Midwest presence."

GC updates its capital modelling tool

Guy Carpenter & Company has launched two updates for its capital modelling tools, MetaRisk and MetaRisk Reserve.

The MetaRisk Reserve 5 update has added an application program interface that embeds within the client's existing modelling interface to automate all aspects of a reserve risk study, which allows the actuary more time for critical analysis.

MetaRisk Reserve 5 also includes the Bornhuetter-Ferguson model, expands aggregation capabilities, and facilitates cloud computing to align with industry trends.

The MetaRisk 9 update meanwhile, will provide "performance enhancements".

Steve White, chief actuary and head of enterprise analytics for Guy Carpenter, said: "As insurance companies in an increasingly complex business environment look for competitive advantage, the updates to MetaRisk Reserve and MetaRisk illustrate Guy Carpenter's commitment to innovation by leveraging improvements in technology and reserving methodologies to provide clients dynamic, easy-to-use platforms to manage capital more effectively."

BNY Mellon launches new platform for medical claims

BNY Mellon has launched a new automated medical claims payment platform for its property and casualty insurance clients.

The bank's new system, using technology from Jopari Solutions, has been integrated into the BNY Mellon Treasury Services payment platform.

It is compatible with medical claim processing systems used in the healthcare industry.

Anthony Brady, head of global product management for BNY Mellon's Treasury Services business, said: "Health care providers are driving the growth for modern payments systems."

"They are looking for efficient systems that reduce costs and payment times and are compatible with regulations governing property and casualty and worker's compensation businesses and medical claim payments," Brady explained.

"This fully automated system is now integrated with our global payments platform to deliver standardised property, casualty and workers' compensation payments."

Do you have a story we should cover?

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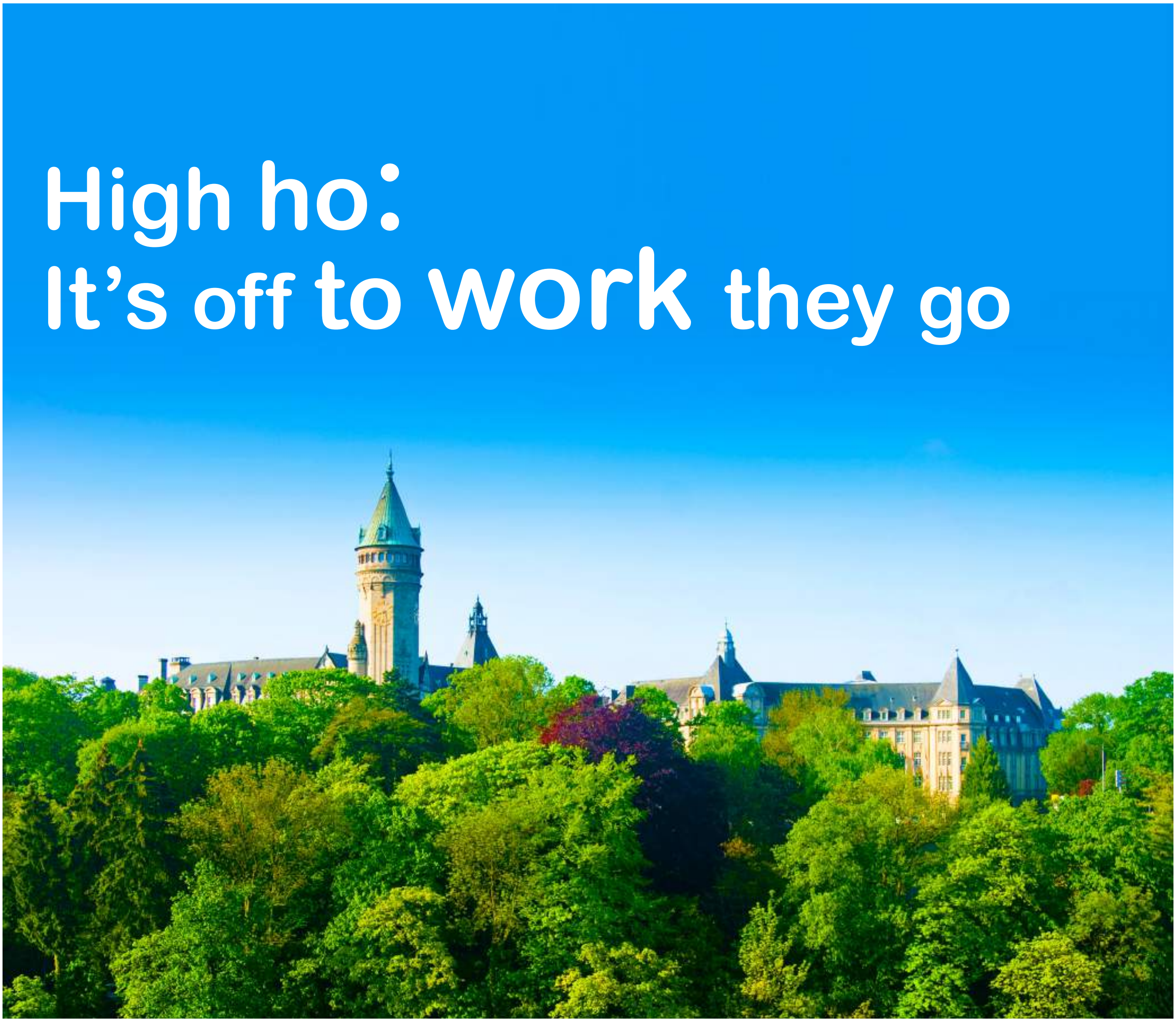
High ho: It's off to work they go



Attendees of the European Captive Forum heard about the many challenges facing the captive insurance industry, but associations suggested working together could allow tools and resources to be shared to overcome them

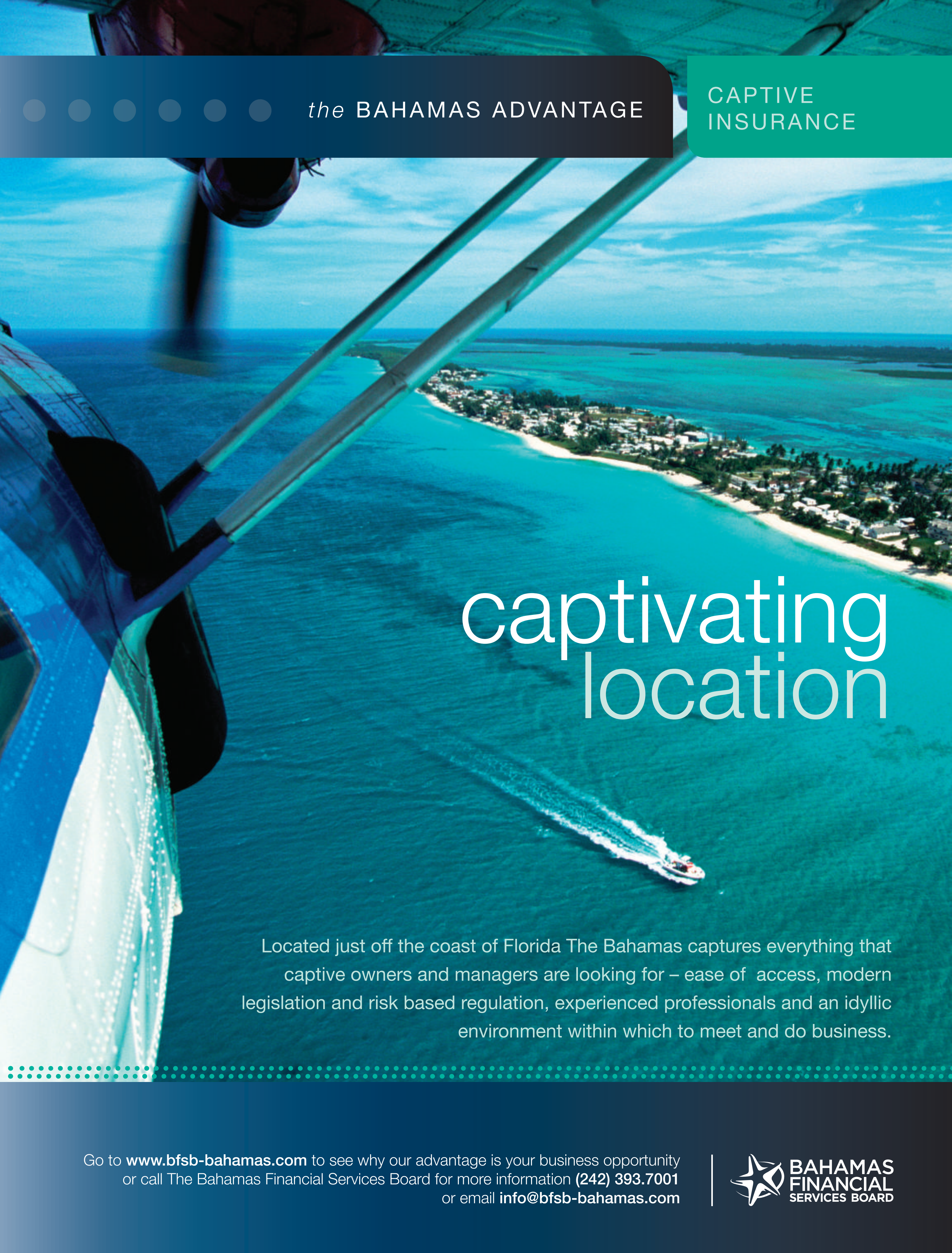
The fourth European Captive Forum, held in Luxembourg and organised by the European Captive Insurance and Reinsurance Owners` Association (ECIROA) and Captive Insurance Companies Association (CICA), gave the European captive industry, and some US representatives, a chance to gather and discuss challenges currently looming over the industry.

Solvency II and the Organisation for Economic Co-operation and Development's (OECD) base erosion and profit sharing (BEPS) package emerged as the biggest causes for concern throughout the event.

In one session, Ciaran Healy, director of consulting for the global captive practice at Willis, explained that the instability driven by these issues has seen a migration of captives to offshore domiciles to avoid Solvency II, while others have moved onshore in order to embrace the directive. He suggested that captives have left European onshore domiciles for the likes of Guernsey or even the US.

Similarly, some captives are considering their substance and location rationale in reaction to BEPS and the potential implications of the UK's exit from the EU.

Healy said: "The result of all this is that there is already some relocation occurring, with many more considering a domicile review. The overall landscape in Europe is going to change. How dramatic that change is going to be we will have to see, but I predict there will be movement."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In his presentation, Healy revealed that 94 percent of captive entities in Europe are located in 'traditional' captive domiciles. Some 63 percent in Europe are not subject to Solvency II.

He went on to say 36 percent of captive entities in Europe are cell captives, while 11 percent of captive entities in Europe are located in the same jurisdiction as their parent headquarters. Healy noted that this last point took Sweden and Switzerland into consideration. If they were removed, the 11 percent figure could drop to approximately 4 percent.

With not many captives located in the same jurisdiction as their parents, Healy pointed out both advantages and disadvantages of home-based captives.

An advantage is that the captive will be aligned with BEPS expectations, he explained, and the substance and economic rationale for location are addressed.

Also, the captive will be embedded to a greater extent within the group, allowing for increased visibility of the captive internally.

On the other hand, a negative implication of domiciling 'at home' is that it requires the captive to operate with a self-managed or semi self-managed approach, meaning less outsourcing availability.

Healy also explained that it could mean a lack of familiarity with the captive business model from regulators, which could consume more time and potentially result in more onerous compliance requirements.

Reasons for captives to steer clear of their parents' domiciles include the fact that captive expertise still focuses around traditional domiciles, which may not necessarily be where the parent is based.

Healy also pointed out that if the home location does not have captive legislation in place, there could be a significant risk associated with being the first to domicile a captive in that location.

He said: "The decision to establish in a non-traditional captive domicile would require a material change in captive strategy, including investment in time, people, processes and systems. Service providers will also need to start thinking about this, as well as everyone in the whole captive lifecycle."

"This trend can be described as a green shoot. There are only two captives that I know that have moved from a traditional captive domicile to their home domicile. I don't think there will be any drastic changes but the figures may change a little bit."

Healy concluded: "BEPS will impact on captives, it will be naive to think it won't affect us. Rightly or wrongly, other offshore locations will be affected. There are equal opportunities for Guernsey and the Isle of Man in the cell captive business. Guernsey is by far the largest domicile in Europe and those captives by large are there to stay."

Solvency II

In another panel discussion, industry professionals called for proportionality and harmonisation in the implementation and enforcement of Solvency II.

Fabrice Frère of Aon Global Risk Consulting focused on the Pillar II requirements. He said that the system of governance for Solvency II must not be seen as simply a "paper" exercise, and noted that there is a level of comfort for captives in being in full control of what is happening.

While captives have always practiced self-governance, the new rules have caused them to approach this more proactively.

But Frère suggested that some regulators are not being proportionate in their governance of captives, noting that many have been "adamant on the implementation of key functions".

Implementing additional requirements for board members and head of key functions can lead to these positions being promoted to 'officer' level, which is unnecessary for a captive, he said.

This could lead to work being completed and checked multiple times, creating inefficiencies in the reporting process.

While accepting that reporting key functions to the board is an important safeguard to make sure Solvency II is followed, Frère said: "I would like to call for proportionality on that."

He added that documentation and clear audit trails are key to this, and suggested that additional scrutiny from external auditors, along with additional disclosures and reconciliations, can quickly become over-burdensome and non-proportionate.

According to Frère, regulators must work with the industry to find the right balance, and a "proactive approach to the regulator does pay off".

He added that "effective" governance is "much more efficient than comprehensive".

With regards to Pillar III requirements, Derek Bridgeman of Marsh Captive Solutions noted that, although it is earlier in the implementation process than Pillars I and II, so far, proportionality in Pillar III has been applied.

There is a risk that this could change, with some domiciles choosing to bring in validation checks at regular intervals.

The Netherlands, for example, is insisting on audit requirements on its reported data, which Bridgeman said has proved "troublesome".

Bridgeman suggested that the regulators should cooperate to publish guidance on how proportionality is being implemented in different domiciles, suggesting that such a comparison could help achieve more harmonisation going forward.

OECD BEPS

Another concern in the captive insurance industry is the OECD's BEPS initiative. Although the plan was released in October 2015, there is still much uncertainty around the impact it is likely to have on captives.

In a session on the transfer pricing principle under the BEPS initiative, Loic Webb-Martin of PwC UK addressed the challenges facing the captive industry coming from the tax authorities, suggesting that the key to success is to be prepared.

He quoted the OECD's definition of the transfer pricing principle, saying: "Commercial or financial relations [must not] differ from those which would be made between independent enterprises."

This means that transactions within a group must be the same as with an outside insurer. However, as captives tend to not offer insurance outside of their own groups, trying to achieve this comparison is "not an easy exercise".

According to Webb-Martin, captives should consider substance, capital, commerciality, allocations, premiums and risks covered. If these issues are all handled correctly, transactions will work as they would with a third party, and "you will be able to prove it to a tax authority".

To prove its activity constitutes a "bonafide commercial transaction", a captive has to be able to prove it has the ability to assume and manage the risks it takes on, and show that the price its insured is paying is 'arm's length', reflecting what is happening in the overall insurance market.

The captive will also have to show that the profit made on the captive is 'reasonable' and relative to the capital required to support the business.

In another session on BEPS, Frère highlighted the country-by-country tax reporting requirements, saying it will trigger audits everywhere.

Captives will face increased scrutiny in these audits, he said, and they must be prepared to answer difficult questions.

Captives must be able to demonstrate that good commercial reasons are behind their existence, and that they have strong governance, and fair pricing, capitalisation and documentation.

Frère said: "Anything that is not documented does not exist."

Another speaker, Praveen Sharma of Marsh, suggested that captives have to evolve with the issues and adapt to changes in regulation, even though some of those in the OECD "don't understand captives".

While tax benefits may once have been the primary reason to launch a captive, and commercial aspects were a bonus, the commercial aspect is now generally the primary reason for a captive and any tax benefits are "the icing on the cake", Sharma said.

Captives must have competent and experienced professionals at a decision-making level to question the validity of transactions, document activity, and consider expected losses, profit margins and expenses, in order to be able to prove their position with regards to commercial viability.

To fight against threats the captive insurance industry is currently battling, the industry's big captive associations suggested that collaboration could be a "powerful tool".

Speakers Udo Kappes and Guenter Droese, representing ECIROA, and Dennis Harwick and Peter Hagnauer, representing CICA and SIRCA, respectively, pinpointed the BEPS initiative as an example of where they can achieve more by working together.

The CICA president referred back to a case in 2008, in which the Internal Revenue Service tried to ban single-parent captives.

The industry joined forces to put a stop to it before the new rule was signed into law. Harwick noted that when a strong coalition comes together it can be powerful.

The benefits of such an approach can include the ability to pool resources, according to Kappes.

He said: "We have already started the approach and we are trying to extend the relationship with other associations such as the Federation of European Risk Management Associations, which also expressed their concern on the BEPS topic." **CIT**

Better than you thought

A captive insurance entity is capable of more than many would expect, according to John Thomson of HAI Group

Often companies, as individual entities or members of affiliation groups, look to a captive insurance solution as an opportunity to minimise costs. Perhaps even looking for the captive solution to consistently cost less than the commercial insurance market alternatives. Not only does captive insurance pricing arbitrage create additional risks for the captive owners, it also exposes the captive insurance entity's financial capital to adverse risk selection, which is ultimately reflected in volatile earnings and potential capital erosion.

A captive insurance programme is established to provide a consistent risk-bearing platform to meet the current and emerging risks of its owners. Traditionally the captive insurance platform addresses issues such as coverage, cost, capacity, claims, and cash flow. Implicit in this is a strategic and long-term view. Success for both the captive insurance entity as well as its owners is not measured in income statement component views alone, but even more importantly—extensive focus on the balance sheet and its components. Hence, the long-term view is essential.

Viewing insurance and risk costs associated with a captive insurance programme as an expense (income statement view) rather than a form of capital (balance sheet view) is not only sub-optimal from a management perspective, it is inappropriate in terms of capital management. Consider this perspective: the insurance contract provided by a captive insurance company provides or introduces financial capital into the business when a covered event occurs. This insurance contract is essentially an alternative form of capital that mitigates the financial impact or volatility associated with a loss or event that might otherwise be uninsured, or the recovery delay or denial of claim from a commercial insurance company.

A captive insurance company is indeed an insurance company

Captive insurance companies face a challenging range of risks and exposures—financial, operational and underwriting. These risks all have significant impacts on the captive's capital and its related costs.

The critical success factors for a captive insurance programme or solution include: a long-term commitment by the captive owner's senior management; a strategic versus quarter-to-quarter financial focus; a commitment to managing risks—both operational and enterprise; a strategic and immunised investment strategy; and a partnership approach.

Remember, when you are forming and owning a captive insurance subsidiary, either as a subsidiary or participating in a group captive, you are entering into the insurance business. With this, you have access to a unique business value proposition, and with this comes a specific set of performance metrics, strategic imperatives, business strategies and corporate/cultural behaviours. To properly manage this business model and manage the capital contained in your own or group-owned insurance entity, there is a set of behaviours and best practices to follow in strategic risk and financial management:

- Develop and communicate clear vision, mission and strategic direction for the captive entity, integrated into the corporate enterprise risk management process. Stick to the plan and do not deviate from core competencies and areas of focus. Specific strategic themes include accountability, sustainability and visibility.
- Follow disciplined underwriting and claim processes in establishing pricing integrity and proper valuation of claim reserves, including case reserves and incurred but not reported development. Utilise appropriate advanced analytics to make determinations and estimates, minimising volatility in financial outcomes.
- Establish underwriting philosophies, practices and procedures to guide risk acceptance and pricing decisions, again, minimising volatility in financial outcomes.
- Ensure financial solvency through rigorous capital management to ensure financial solvency and ability to meet contractual obligations to policyholders and stakeholders.
- Conserve and manage valuable capital resources, in all forms.
- Establish a risk management culture that guides behaviours and ensures appropriate risk appetite and tolerances, as well as achievement of strategic objectives.
- Promote teamwork and leadership, and ensure rewards for the right behaviour.

Following these guidelines and best practices will: help to ensure that the long-term strategic and financial viability of your risk bearing entity or company; provide sustained relevance and alignment of the captive insurance operations, products and services; allow a solid foundation for the regulatory and compliance requirements; and enhance the financial performance of your overall enterprise.

In addition, it will provide a vehicle for the emerging risks and additional business opportunities for your organisation, and the ability of your captive insurance company to support your corporate financial and strategic directions.

In essence, your captive insurance entity can be an active company within your corporate structure and could actually be more that you thought it is capable of being. **CIT**

John Thomson
President and CEO
HAI Group

Information captured from big data can give clients an insight into which areas of exposures they could benefit from, specific to their industry sector. Warren Vickers of CapSure explains

What common trends are you seeing in workers' compensation? What about in medical stop-loss claims?

Workers' compensation: Business owners and shareholders have become very aware of the litigious environment that we live in. As a result, they have had to adapt by implementing extremely sound safety policies and procedures within their businesses. The safer business practices have begun to lower their workers compensation claims, thus allowing them the opportunity for the first time to significantly profit from their own safe behaviour through setting up a captive insurance programme.

Medical stop-loss: Commercial insurance brokers possess a major business opportunity to use purpose-built insurance companies that provide medical stop-loss insurance to their current clients who have self-funded health insurance plans. The broker gets to participate in the underwriting profit and investment income from the health plans they are administering, rather than passing those profits on to a commercial stop-loss insurance carrier. With efficient underwriting, brokers can generate significant additional revenues. These are in-house revenues they are currently passing off to commercial stop-loss insurance carriers.

Have you seen an increase in workers' comp and/or medical stop-loss claims?

Workers' compensation: CapSure Risk has very thorough underwriting assessments, claims review and processing controls for each of our worker compensation clients. We help programme members develop workplace policy guidelines to further assist them in creating a safer working environment. Our captive programmes have performed very well and claims experience has been lower on average.

Medical stop-loss: Our medical stop-loss programmes have traditionally lower claims history on average. Our underwriting assessments, claims review and processing procedures are very efficient and streamlined, and this allows our captive programme to perform extremely well.

How is data used to help captives reduce losses in workers comp?

Our data analytics tools allow us to analyse each prospective client's business and determine areas of risks within the specific business, as well as areas of risk within the industry sector.

This information provides our clients valuable insight into their current risks, as well as what types of unforeseen risks they may encounter in the future based on their industry sector.

The data gives our business clients a head start to develop procedures that will efficiently and effectively deal with any future incidents, which consequently lowers their overall exposure.

A lot of our day-to-day operations have become streamlined through automating certain areas of our business which allows us more face time interaction with our client base.

How is technology evolving to help captives manage with all of the data available?

The diversity of information that we are able to capture through the evolution of big data provides us opportunity to perform detailed analysis on each prospective and current captive client, to determine exactly what areas of exposure they could benefit from based on their unique business and their specific industry sector.

This helps our clients' businesses to save money by eliminating unnecessary and expensive coverages currently bundled into their existing traditional insurance policies. **CIT**

Industry Events

Cayman Captive Forum

29 November - 1 December
Grand Cayman
www.imac.ky

More than 1,400 specialists including captive directors, CFOs, risk managers, service providers and captive managers from around the world will converge in the Cayman Islands to discuss the issues most pressing to the captive insurance industry. This is the event to connect, learn and share insights and best practices.

ILS: The New Opportunities

5 December
London
www.cityandfinancialconferences.com/ils

The purpose of this conference is to look at UK ILS proposals and the opportunities and challenges they will involve. The event will include panel sessions and presentations from all the significant market players. There will be speakers from the UK Treasury and the relevant financial authorities and discussion led by the London Market Group, the industry body that has been helping spearhead the initiative.

JLT Insurance Management (JLTIM) has appointed Anne Marie Towle as executive vice president and captive consulting practice leader, effective 1 January.

Towle was previously senior captive consultant and senior vice president for Willis Towers Watson. She was responsible for sales, business development, marketing and branding for the company's captive insurance practice in North America.

Guy Ragosta, CEO of JLT, said: "JLTIM has grown significantly, and we believe Anne Marie Towle will help us continue to grow. We are delighted to welcome a professional of Towle's calibre to the JLTIM team."

Towle added: "I am extremely excited to join JLTIM, and I look forward to working with its talented group of professionals."

Capita Employee Benefits has expanded its senior investment team, adding three new hires to its investment consultancy practice and promoting one existing team member.

Chris Gill and Hiten Nandha have both joined as senior investment consultants. Prior to their new roles, Gill served at Mercer and Nandha worked at Willis Towers Watson.

Another addition to the team is Brendan Coffey, has joined from Unilever, taking on the role as head of investment strategy.

Finally, Tom Hawthorn, who was previously senior investment consultant, has been promoted to the role of head of manager research.

Bobby Riddaway, head of investment consulting at Capita Employee Benefits, commented: "Chris Gill, Hiten Nandha, Tom Hawthorn and Brendan Coffey strengthen and complement the existing senior investment team."

He added: "These appointments help to demonstrate our commitment to providing outstanding investment solutions to our clients."

Stephan Vieira has joined the Beazley specialty surety treaty unit as a reinsurance underwriter, in the firm's Miami office.

In his new role, Vieira will underwrite surety insurance programmes in Latin America and Caribbean.

He joins Beazley from Transatlantic Reinsurance Company, where he served as vice president for treaty surety and credit underwriting.

Jo McCann, head of specialty treaty at Beazley, said: "I am delighted to welcome Stephan Vieira as we expand the geographies across which we provide surety reinsurance solutions."

FiscalReps senior client manager Christophe Bourdaire has moved from the UK to France.

He will focus on supporting the company's growing European client base and will strengthen its European expansion.

Bourdaire said: "I am excited about the opportunities that this move will bring."

"FiscalReps has a growing client base in France and by being physically located there I will be able to work more closely with our clients."

Bourdaire joined the company in 2012 and manages an extensive portfolio of international clients, with most hailing from French speaking countries. CIT

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