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Florida modifies captive insurance law

TALLAHASSEE 28.05.2013

Florida has introduced a new bill revising the state's 2012 captive insurance law.

Committee Substitute for House Bill 1191 (CS/HB 1191) makes a number of changes intended to address any unintended consequences that may have resulted from the 2012 law.

In 2012, the Florida legislature passed Committee Substitute for House Bill 1101. The bill—that came into effect on 1 July 2012—made significant changes to captive insurance law in the state.

Current law states that industrial insured captive insurance companies can only insure the risks of the industrial insureds that comprise the industrial insured group and their affiliated companies.

According to the Florida Senate's website: "[CS/HB 1191] broadens the entities that an industrial insured captive insurance company is allowed to insure to include the industrial insureds' and affiliates' stockholders or members, and affiliates thereof, or the stockholders or affiliates of the parent corporation of the captive insurance company."

Bill CS/HB 1191 also allows an industrial insured captive insurance company with unencumbered capital and surplus of at least $20 million to be licensed to provide workers' compensation and employer's liability insurance in excess of $25 million in the annual aggregate.

Furthermore, the bill makes pure captive insurance companies responsible for adopting risk management standards for controlled unaffiliated business. The bill requires such pure captive insurers to submit these standards to the Office of Insurance Regulation for approval.

"This approach provides pure captive insurers with more flexibility than current law, which requires the Financial

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CITINBRIEF

Missouri passes segregated cell legislation

Missouri Governor Jay Nixon has signed Senate Bill 287 into law, allowing for the formation of sponsored captive insurance companies or segregated cell captives in the state.

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BMA restructures senior management team

The Bermuda Monetary Authority (BMA) has realigned its senior management team to improve cost efficiencies and increase Bermuda's appeal to new market entrants.

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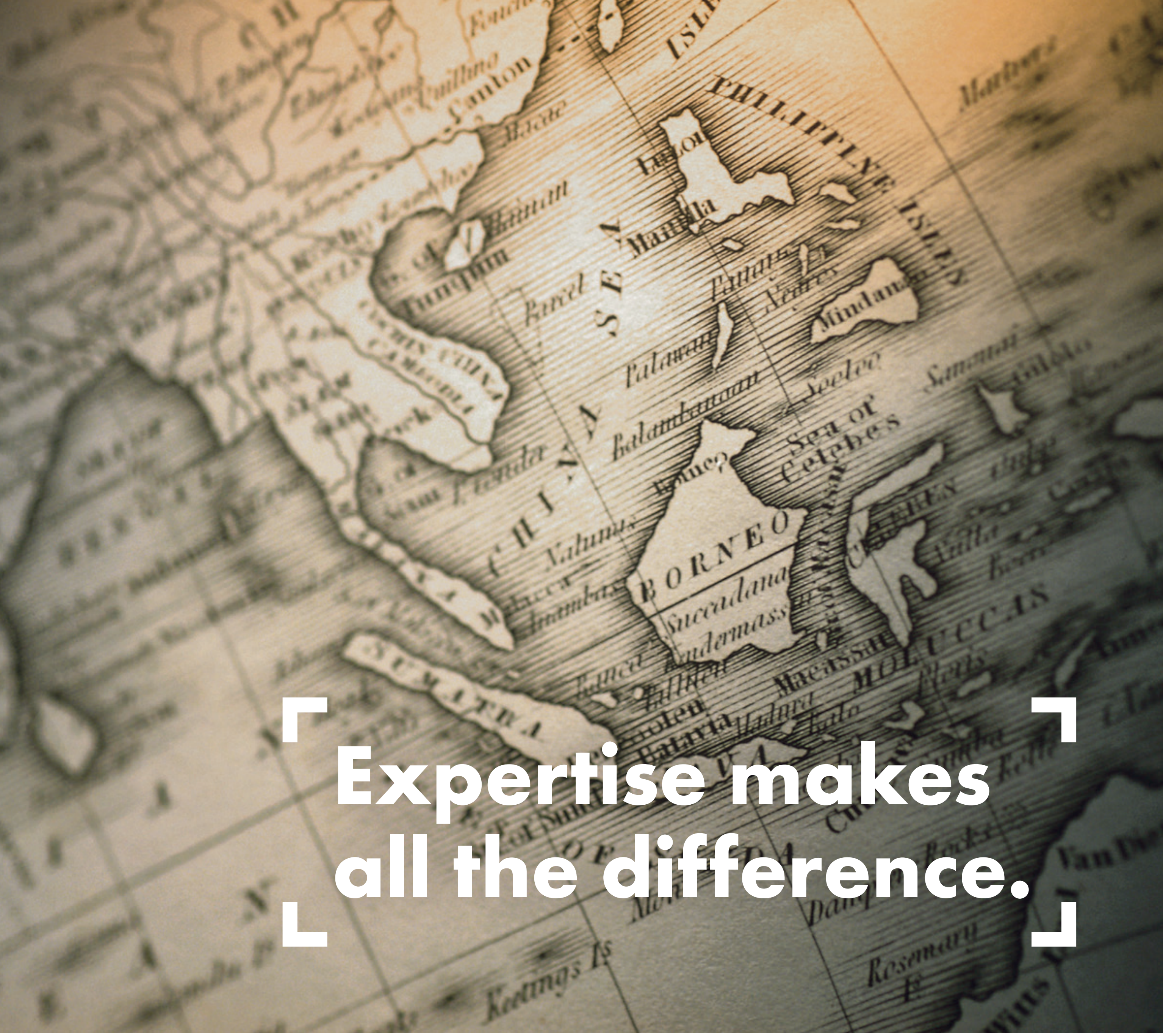

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Florida modifies captive insurance law

Continued from page 1

Services Commission to adopt such risk management standards by rule."

"Finally, the bill corrects any inconsistency in current insurance law by exempting captive insurance companies from deposit requirements that now exceed the surplus requirements to for a captive," said an analysis by House of Representatives staff.

CS/HB 1191 has been approved by the Senate and House of Representatives and is currently awaiting the governor of Florida's approval.

If approved, the provisions will take effect from 1 July 2013.

Missouri passes segregated cell legislation

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The bill is intended to help lower the overhead costs for mid-sized businesses in Missouri that self-insure through captive insurance companies, and to encourage more captives to form in the state.

Under the new act, a sponsored captive insurance company will be incorporated as a stock insurer with its capital divided turned into shares and held by stockholders, as a mutual corporation, as a non-profit corporation with one or more members, or as a manager-managed limited liability company.

The act also allows sponsored captive insurance companies to establish one or more protected cell companies to insure risks under certain conditions.

The effective date for the new legislation is 28 August 2013.

BMA restructures senior management team

Continued from page 1

Marcia Woolridge, director, will manage the banking, trust corporate services and investment division. She will add supervision of businesses licensed under Bermuda's new corporate services providers regime to her responsibilities.

Woolridge's new responsibilities are in addition to her supervision of the banking trust, investment fund, fund administrators and investment businesses sectors.

Shelby Weldon will expand his role as director to include the licensing and authorisation functions for all non-insurance entities. In addition to captive and commercial insurers, he will be responsible for licensing and authorisations for banks, investment businesses, investment funds, trust companies and corporate service providers.

Current director Shanna Lespere will assume responsibility for areas of the BMA's operations function, including finance and currency operations, human resources, research, facilities, programme management and enterprise risk management.

Finally, Shauna MacKenzie's role as director will now encompass responsibility for the authority's regulatory policy function. She will also be responsible for legal services, and development and application of the BMA's enforcement framework.

Jeremy Cox, CEO of the BMA, said: "The restructuring and re-assigned responsibilities within the senior management team support the BMA's work to implement Bermuda's supervisory regimes even more effectively."

"We are successfully working towards achieving our focused vision for efficient, forward looking risk-based supervision as the market continues to evolve. Just as important, the changes also support sharing of our in-house technical skills across the market sectors we supervise, fostering a multidisciplined, coordinated supervisory approach."

East meets West with new captive programme

Eastern Alliance Insurance Group, a subsidiary of Eastern Insurance Holdings, and Westfield Insurance have formed EastWest Alliance, a multi-line captive for mid-to large-size employers.

EastWest Alliance offers a multi-line product, including workers' compensation, general liability and commercial automobile coverage.

The EastWest captive programme is domiciled in the Cayman Islands through Eastern Reinsurance, a subsidiary of Eastern Insurance Holdings.

Michael Boguski, president and CEO for Eastern Insurance Holdings, said: "The [EastWest] programme provides a long-term, stable market solution backed by two well-respected regional carriers rated "A (Excellent)" by A.M. Best Company."

"Eastern Alliance will underwrite the workers' compensation line and bring their proven specialisation in underwriting, risk management and claims administration. Westfield will underwrite and provide their respective proven expertise in underwriting, risk management and claims administration for the general liability and commercial auto lines of business."

Sooner Insurance gets rated

A.M. Best has affirmed the financial strength rating of "A (Excellent)" and issuer credit rating of "a" of Sooner Insurance Company, based in Burlington, Vermont.

"The ratings are based on Sooner's excellent capitalisation, history of consistently producing net underwriting income and net income, as well as being the captive insurer for its ultimate parent, ConocoPhillips," said A.M. Best in a statement.

The ratings also consider the parent's overall risk management strategy and Sooner's core involvement in this strategy.

Partially offsetting these positive rating factors is the possible change in Sooner's net retentions that could happen year over year, as well as the limited diversification of business written, which is expected with a single parent captive.

A.M. Best is unlikely to upgrade Sooner's ratings over the long term due to its limited market profile.

Key factors that could lead to rating downgrades are a significant loss of surplus, consistent adverse reserve development and/or a significant change in Sooner's risk profile.

Jupiter Insurance ratings are out of this world

A.M. Best has confirmed the financial strength rating of "A (Excellent)" and issuer credit rating of "a" of Guernsey-based, Jupiter Insurance.

Jupiter Insurance is a captive of international oil and gas company, BP.

The ratings reflect Jupiter's strong underwriting performance as well as its strong risk-adjusted capitalisation.

"Offsetting these positive rating factors is Jupiter's high level of risk retention, as well as its concentrated investment portfolio, which primarily contains financial instruments linked to its parent, BP," said the rating firm in a release.

Greater tax transparency needed, says Guernsey chief minister

Guernsey Chief Minister Peter Harwood has set out the island's leadership and track record on tax transparency, ahead of the G8 and G20 meetings on the subject.

In a statement, Harwood explained that common global standards are the most effective method of fighting fraud and tax evasion.

Harwood said: "Guernsey has welcomed the recent announcement by the UK, along with France, Germany, Italy and Spain, to pilot automatic information exchange based on the FATCA [US Foreign Account Tax Compliance Act] agreements with the US (the G5 Pilot) and we support those countries' efforts to ensure that the OECD adopts multilateral automatic information exchange as a new global standard."

"Earlier this year I was able to announce Guernsey's intention to finalise a draft agreement on a proposed 'tax package' with the UK. That package included an agreement in principle to enhanced reporting of tax information along FATCA principles."

He added: "Our agreements with the UK and the US will be subject to the proper decision-making process of our Parliamentary Assembly and will be presented to them for approval later this year. As I made clear in my open letter to Prime Minister David Cameron of 1 May 2013, at that juncture I would be willing to present a report and a recommendation on joining the G5 Pilot."

Harwood went on to say that the actions taken in Guernsey emphasise that the island fully supports international cooperation on the transparency of and access to beneficial ownership information.

"We support the calls for greater tax transparency—not just with our words but with our actions. We are part of the tax transparency process, and look forward to continuing to play our part. The message from Guernsey is clear—Guernsey is not a jurisdiction of choice for those who want to hide."

Fitch rates Black Gold Re

Fith Ratings has affirmed the Insurer Financial Strength rating of "BBB" to Black Gold Re. The rating outlook is positive.

Black Gold Re's rating as a captive company reflects its linkage and strategic importance to its parent, Empresa Colombiana de Petroleos—Ecopetrol.

The rating also reflects Black Gold Re's adequate technical performance, high captialisation, low leverage and strong liquidity ratios.

"The rating outlook is positive. An upgrade may be considered due to positive changes in the credit profile of the parent … Key ratings triggers that may lead to a downgrade include a decrease in Ecopetrol's availability and willingness to provide support," said the rating firm in a statement.

Guernsey signs DTA with Luxembourg

Guernsey has signed a double taxation arrangement (DTA) with Luxembourg.

Gavin St Pier, Guernsey's treasury and resources minister, signed the bilateral DTA with Luxembourg of 10 May with Luxembourg's Chargé d'Affaires to the UK, Béatrice Kirsch.

St Pier said: "This is an important further component in Guernsey's network of tax agreements. Following on so closely from the signing of our DTA with Hong Kong, it is further demonstration of Guernsey meeting the highest global standards of international tax cooperation."

Fiona Le Poidevin, chief executive of Guernsey Finance, said: "There is already a strong link between Guernsey and Luxembourg in relation to financial services business and this is particularly the case with investment funds, where many platforms will have structures in both jurisdictions."

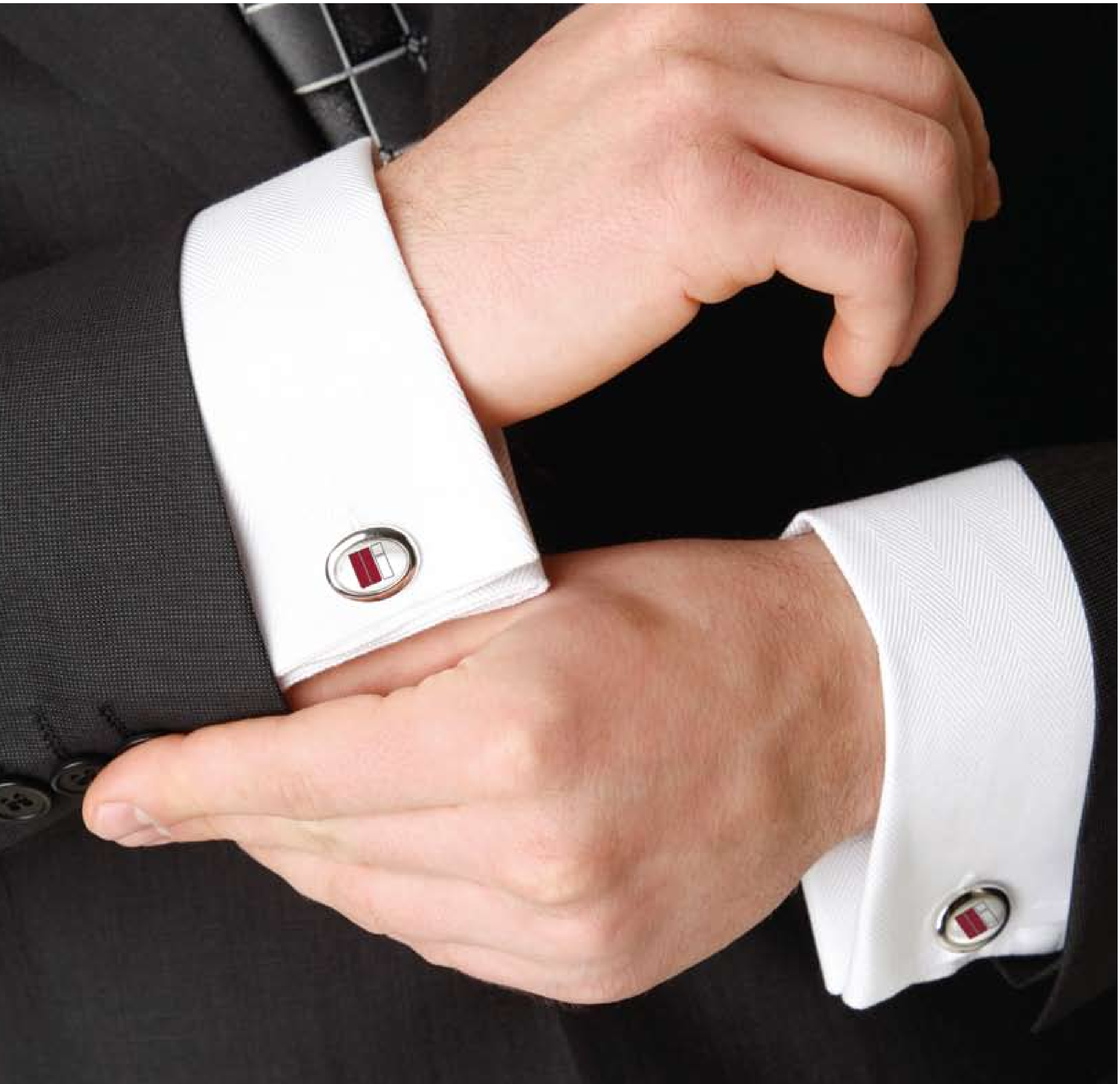
"The DTA means that individuals or companies with 'home' as one jurisdiction but with interests in the other jurisdiction will have mechanisms in place to prevent them from being taxed by both sets of authorities on the same income."

The latest signing means that Guernsey has now signed full DTAs with eight jurisdictions. It most recently signed arrangements with Malta, the Isle of Man, Jersey, Qatar and Singapore.

St Pier also signed a tax information exchange agreement (TIEA) with Botswana at the Botswanan High Commission. A further TIEA with Swaziland is expected to be concluded in the near future.

Medical RRG achieves superior rating

A.M. Best has affirmed the financial strength rating of "A++ (Superior)" and issuer credit



rating of "aa+" of The Medical Protective Company and its two reinsured affiliates, MedPro RRG and AttPro RRG Reciprocal.

"The ratings reflect Med Pro's excellent capital strength, strong national business profile and extended trends of favourable operating performance."

"The company's continued outstanding underwriting performance is driven by disciplined underwriting standards, conservative reserving practices and a proactive claim handling philosophy," said A.M. Best in a statement.

The positive ratings are also attributed to the support provided by Med Pro's ultimate parent, Berkshire Hathaway.

Partially offsetting the positive ratings are Med Pro's product concentration in the highly cyclical medical professional liability market and its above average concentration levels in select investments.

MetLife brings captives back onshore

MetLife is merging its offshore captive business into US-regulated entities, after regulatory powers cracked down on offshore captives.

It is a strong statement from the corporation, which is one of the largest global providers of insurance, annuities, and employee benefit programmes, with 90 million customers in more than 60 countries.

The reason for the onshore move comes from an August 2012 letter, when New York cracked the whip on captives, as well as the continuing effort to reduce its risk profile in its variable annuity business.

The New York Department of Financial Services sent letters to 80 insurance companies, including MetLife, regarding their handling of captive insurance companies in an attempt to gain full disclosure about captives' financial health.

The companies were required to respond to the missive from the state inquiry by 8 August, with state officials expressing concern that the captive arrangements may give a false impression of the insurer's financial health, particularly in cases where the captive is funded using a letter of credit that allows the bank to hold the parent company responsible for the debt.

After this warning, MetLife made its disclosure at the annual investor's day presentation in New York, and in a filing with the Securities and Exchange Commission (SEC).

Officials said they are merging three US life insurers with their Cayman Islands-based reinsurance captive in the hopes of creating a larger, well-capitalised US life company.

MetLife chief executive Steven Kandarian led the discussion, which first illustrated the recent change in the GMIB MAX V product, where MetLife changed the guaranteed minimum income benefit, its largest selling rider benefit.

The roll-up rate was reduced to 4 percent, and the withdrawal rate was lowered 0.5 percent to 4 percent. It was stated in the presentation that the changes were vital to the firm's overall risk profile.

Kandarian also accepted that the New York inquiry played a part in the decision: "I should note at this point in time, the New York Department of Financial Services' industry inquiry regarding captives was an important factor in our taking a closer look at our offshore reinsurance subsidiary."

He added that the firm also considered the US Dodd-Frank Act's affect on collateral for derivatives when deciding to bring businesses back onshore.

EC looks for comment on European disasters

The European Commission has released a green paper that questions the adequacy and

availability of appropriate disaster insurance in the face of natural and man-made disasters.

With the green paper, the European Commission aims to raise awareness and assess whether or not action at EU level could be appropriate or warranted to improve the market for disaster insurance in the EU.

The paper states that between 1980 and 2011, the economic toll of natural disasters in the whole of Europe approached €445 billion in 2011 values.

Günter Dröse, chairman of the European Captive Insurance and Reinsurance Owners Association, said: "Insurance and risk transfer is the last instrument once all other risk prevention and mitigation tools have been implemented, in this field companies and public sector have to invest more heavily to avoid or protect disastrous impact caused by natural events."

According to Dröse, one option may be for companies to set up specialised captives owned by state/public sectors "to provide capacity and/or alternative risk transfer structures in combination with the market capacity provided by the traditional insurance market".

"I personally would suggest captives (and their owners) to check all options which are available to place sufficient sum insured in the traditional as well as in the non-traditional market. Cost considerations will be just one factor within the decision making process."

The commission invited stakeholders to comment on the issues set out in the green paper and respond to questions raised. The consultation is open until 30 June.

Brown & Brown to buy Beecher Carlson for $336.5 million

Brown & Brown has agreed to purchase its rival Beecher Carlson.

The deal, which is expected to close in July, will net Beecher Carlson owners Austin Ventures, FSPM and a group of individual employee and non-employee equity holders $336.5 million.

In Beecher Carlson, Florida-based US retail broker Brown & Brown is buying an insurance and risk management broker with operations that include captive and programme management.

As a part of the deal, Beecher Carlson president Steve Denton will be named a regional vice president at Brown & Brown. He will also serve as the CEO of Beecher Carlson. Dan Donovan, the firm's current CEO, will become its executive chairman.

Both Denton and Donovan will actively participate in the day-to-day operations of Beecher Carlson. They will also join Brown & Brown's leadership council.

In a statement, Powell Brown, CEO and president of Brown & Brown, said: "This transaction brings many exciting opportunities to Brown & Brown. Beecher Carlson enjoys an enviable position in the industry segments in which it operates, especially in the large account space. We are bringing together great people and a shared customer service and sales culture."

Speaking during a conference call to confirm the deal, Donovan said: "[Everyone shares] excitement for the new platform that Beecher Carlson will operate under."

Jason Flaxbeard, who leads the Beecher Carlson hospitality practice and captive/alternative risk transfer operations throughout the US, Bermuda and the Cayman Islands, said that his firm's "marriage to Brown & Brown will be a good one".

"I don't expect anything to change for captive management—there will be a lot of opportunities in the future."

He went on to say that he will work on the firm's captive proposition in the coming weeks so that the potential for investment and growth can be assessed.

Beecher Carlson earned $105 million in revenue last year.

Bermuda captive gets A ratings

A.M. Best has awarded the financial strength rating of "A- (Excellent)" and issuer credit rating of "a" to Ardellis Insurance, based in Bermuda.

Ardellis's ratings reflect its conservative underwriting leverage, strong level of capitalisation and profitable operating results driven by its underwriting performance.

The ratings are partially offset by Ardellis's relatively high retention and limited profile as a single parent captive of Universal Forest Products.

Ardellis provides coverage for general liability, auto liability, workers' compensation, property and medical stop loss. It also assumes minor medical stop loss exposure from third parties.

"Rating drivers that could lead to a positive outlook and/or an upgrading of Ardellis' ratings are material and sustained improvement in its underwriting performance and capitalisation. Additionally, improved overall risk management and reduced overall net exposure could lead to an upgrading of the ratings," said the rating firm in a release.

Physician Insurers Association of America rebrands

The Physicians Insurance Association of America has made a number of changes to its organisational brand to support and build on the association's role in medical professional liability.

The association will now do business as PIIA. To accompany the new name, PIIA has also created a new tagline: "Our expertise is medical liability. Our passion is quality healthcare".

The PIIA is also unveiling a new logo and launching a redesigned website to reflect its expanding role in the medical professional liability space.

Brian Atchinson, PIAA president and CEO, said: "We are committed to ensuring that PIAA remains an indispensable resource for every group with a commitment to quality healthcare and a stake in medical professional liability regardless of structure—mutual, reciprocal, RRG, captive, stock, or trust."

"And PIAA will continue to offer programmes and services tailored to meet the needs of all types of healthcare providers and healthcare systems covered—physicians, hospitals, nurses and nurse practitioners, dentists, or others."

Toyota captive moves up the ranks

A.M. Best has upgraded the financial strength rating to "A (Excellent)" and the issuer credit rating to "a" from "a-" of Toyota Motor Insurance Company (TMIC). The outlook for both ratings has been revised to stable from positive.

In a recent statement, A.M. Best said: "The ratings reflect TMIC's excellent risk-adjusted capitalisation and consistently strong operating results driven by underwriting income and complemented by a steady flow of investment income."

The positive attributes are further supported by TMIC's solid cash flow, liquidity and leverage metrics. TMIC also benefits from the support of its ultimate parent, Toyota Motor Corporation.

TMIC plays a strategic role within the Toyota organisation by providing vehicle service agreements, guaranteed auto protection agreements and excess wear and use coverage sold through Toyota, Lexus and affiliated dealerships throughout the US.

The hard sell

CIT chats to Thomas Adams and Alex Webb of the North Carolina Captive Insurance Association to find out how the new domicile on the block is progressing

JENNA JONES REPORTS

What will the NCCIA focus on in the coming months?

Thomas Adams: The NCCIA will be focused in the short term on educating businesses that there is a new in state tool for them to use in considering how to meet their insurance needs, using the captive insurance model. There has been strong interest from businesses in the bills' progress and much of our effort will be directed toward educating businesses on the specifics of the legislation and how it may benefit their activity.

When do you think bills HB 473 and SB 476 will make it through Congress?

Alex Webb: HB 473 and SB 476 will be merged into one bill in the near future. Currently HB 473 is in the Senate Insurance Committee where we expect some technical amendments. On final passage, we expect it will contain the current content plus some of the technical changes. Upon adoption it will be a state of the art framework for regulation of captive companies in North Carolina.

How much support is there for North Carolina becoming a captive domicile?

Adams: The two bills moving through the legislature have initially passed both houses without a dissenting vote. That is very rare and indicative of the strong support in the state for North Carolina to be a key domicile for captives in the US.

North Carolina's department of insurance and legislature are all very excited about the law. The goal is to become competitive with the active captive domiciles. The state understands that this is a competitive environment and they are ready. The law is state of the art legislation and it includes meaningful funding. There are also some differences from established captive domiciles, one example is the fact that North Carolina will not charge fees.

Is the US becoming too saturated with domiciles, and why?

Webb: While more than 30 states allow captives, only a handful have aggressively marketed their regulatory frameworks.

The intent of the North Carolina legislation is for the state to aggressively market itself and subsequently become a key home for captive companies.

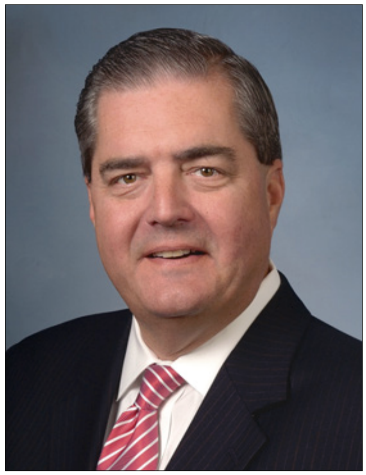
As a new US domicile, what will North Carolina offer that other domiciles currently do not?

Webb: North Carolina's law is being crafted in such a way that it is friendly to businesses that want to pursue the concept. It is seen in the legislature as an economic development tool. Businesses will need to compare this law to others. We believe when they do, North Carolina will be a very strong competitor to locate their captive.

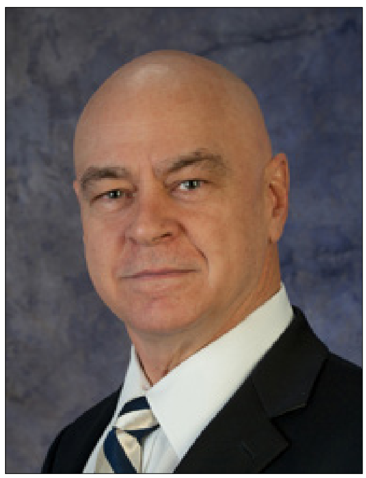
We understand that this is a competitive environment, however, we are ready. As stated earlier, there are no fees in the proposed law. The law also does not require the state to perform audits at stated intervals, and in fact consideration can also be given to waiving the audit requirement under certain circumstances. The premium tax structure is competitive. North Carolina clearly understands that it is to a great degree about service and commitment and we believe that we will be able to demonstrate both.

How does the NCCIA plan to market North Carolina to attract captive business?

Adams: Over the next year, NCCIA will ramp up its efforts to attract members by offering seminars and an annual conference/exhibition. We will also participate as presenters at annual meetings of other trade associations. We also expect outreach efforts from the North Carolina Department of Insurance. CIT



Thomas Adams
President and CEO
NCCIA



Alex Webb
Chairman
NCCIA

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I depend on expertise

CSI International Underwriting's David Roberts and JS de Jager tell CIT why being an independent company is integral to managing captive clients

MARK DUGDALE REPORTS

Considering the current strength and market presence of the large broker-owned managers, how do independent managers continue to attract captive insurance business?

David Roberts: Inevitably, the large broker networks will attract a significant proportion of the available business. However, independent managers have seen a great number of new licences coming through and there will always be a place in the market for bespoke offerings and a more tailored service than the large operators can provide.

JS de Jager: Clients really appreciate the close personal and business relationship that can only be delivered by smaller organisations. A large network of accessible professionals enables CSI to provide products and services that can be custom-made to meet the client's particular needs.

In a marketplace that is dominated by large brokers ever expanding through mergers and acquisitions, your independence could be a real boon?

de Jager: It certainly is. CSI enjoys excellent relationships with clients. They know that they will have continuity in the people that they deal with and a consistent approach to their business. We tend to find that it becomes a personal as well as a business relationship. Larger providers, with regular staff turnover and restructuring, just can't give that degree of focus. Because we are independent, we are not tied to in-house service providers or to contracted service providers. We can go to the specialist best suited to the client's needs and circumstances. In doing that, we will work with the client, so that they are actively involved in the selection process and can make sure that their voice is heard. CSI works with external service providers in the US and elsewhere, selecting the most appropriate one on a case-by-case basis.

Presumably, this leaves you to concentrate on your core areas of expertise?

Roberts: Exactly. You don't need to be big in order to provide a complete service. Working with external service providers enables CSI to deliver a comprehensive package to the client that is focused on the client's overall requirements. The whole process is driven by the client's needs, not the service provider's systems, in-house services and already selected and contracted specialists—we don't do 'one size fits all'.

Surely one of the perils of being independent is that you lack the consultancy and brokerage network that can provide you with new business sources?

Roberts: This may be true to a degree as our competitors that form part of large brokerage networks automatically benefit from a passive flow of new business introductions. This being said, CSI has developed over the years a strong network of independent service providers with wide ranging expertise enabling us to tailor our services as may be required on a client by client basis.

de Jager: Many independent managers do work closely with firms of regional brokers that benefit from a Cayman connection. By nature, the regional brokers may be uncomfortable in having their client business managed by a primary competitor and place great value on having access to alternatives that are accommodating to their and their clients' requirements.

Might some conclude that independence precludes a diverse book of business?

Roberts: Quite the opposite! As an independent manager, CSI has always had a wide spread of business and we would expect this to be common among other independent managers.

Do independent managers worry about consolidation within the industry?

Roberts: As in many areas, consolidation seems to be a major theme and it is inevitable that further consolidation with take place. Constant acquisition will mean that larger offices will continue to hold a large market share of the business. However, independents like CSI will continue to offer choice and an alternative approach. Being a somewhat smaller pond, we are more aware of, and attentive to, the fish!

de Jager: Competing with the larger companies is a genuine challenge for independent managers, but there will always be clients that value the individual approach and personal attention provided by CSI and most other independent offices.

How does CSI set itself apart from the competition?

de Jager: It is the hallmark of CSI that we are able to operate to our own high standards. It comes from our ability to treat our clients as individual businesses, not as part of an amorphous mass where they just get lost in the crowd. Larger organisations inevitably drift towards an internal set of achievement goals and priorities, because that's how staff are judged. As an independent manager, CSI treats clients as individuals with specific and uncorrelated needs, enhancing the close business and personal relationship at all times. We will always strive to achieve the best outcome for our clients, rather than being hidebound by internal structures, reporting systems, targets, goals and so forth that bedevil larger organisations.

Is Cayman seeing a particular type of new business arriving?

Roberts: Within the context of the current prolonged, and continuing, soft market, Cayman is still seeing new licences for all areas of risk, with continuing emphasis on the popular and strong healthcare sector. Another area of significant growth in Cayman is in the use of Segregated Portfolio Companies (SPCs). The increasing interest in new formations and SPCs has been helped even further by legislative changes and the formal implementation of the new Insurance Law at the end of 2012, giving a more flexible approach to licensing and regulation, without reducing the high standards that Cayman sets for itself.

That situation is further enhanced by the industry-advancing regulations being tabled in 2013. In particular, the new Portfolio Insurance Company introduced by the new regulations offers far greater flexibility in the management of assets and risk.

Will there be any further changes in regulation?

Roberts: The regulation of the financial sector in the Cayman Islands through the Cayman Islands Monetary Authority (CIMA) is widely recognised as being to a very high standard, not least in the insurance sector. We should expect constant review of regulations, but CSI anticipates that the key regulatory developments in the immediate future will be more in the line of the further introduction of clear policy statements to further enhance our reputation as the captive insurance jurisdiction of choice. Many of the procedures that are already entrenched in the way that licencees operate and control their businesses have been and are in the process of being formulated and put into published policy statements and formal regulations. This is a general undertaking of CIMA for all areas of the financial sector in Cayman.

de Jager: With regards to the insurance sector, the updating and issuing of these policy statements and regulations have been and, in the main, will be, considered a positive step forward, generally formalising what has always been accepted as informal practice. Regulation in Cayman has traditionally been intended to promote business, while providing proportionate oversight and reporting.

Roberts: Cayman stands out as the domicile of choice for captive programmes. CIMA and other regulators, in light of an overall increase in regulation and know your customer procedures, are committed to compliance while still maintaining an open and welcoming approach to new business. Regulation in some jurisdictions is a burdensome cost-generator that interferes with business. CSI believes that CIMA has traditionally maintained a careful balance between ensuring effective regulation on the one hand, while at the same time avoiding unnecessary impositions on the industry that strangle innovation and cause untenable cost burdens. **CIT**

David Roberts
Managing director
CSI International Underwriting (Cayman) Ltd

JS de Jager
Senior account manager
CSI International Underwriting (Cayman) Ltd

Staying power

CIT takes a closer look at Bermuda to see how the oldest captive domicile is faring after more than 50 years in the business

JENNA JONES REPORTS

In the 1950s, the 'father of captive insurance', Fred Reiss, coined the phrase 'captive' when forming the Steel Insurance Company for Youngstown Sheet & Tube Company.

In 1962, Reiss formed the International Risk Management—incorporated in Bermuda by a special act of parliament—introducing captive insurance to the island.

As the figures show, Bermuda has been an active captive domicile for more than 50 years. According to Lawrence Bird, president of the Bermuda Insurance Management Association, Bermuda's captive industry began when alternative solutions were needed to offer an alternative to an inflexible commercial insurance market.

He says: "Since then, Bermuda quickly established itself as a captive insurance centre and has been the largest captive domicile ever since. This remains the case today and this is expected to continue for the foreseeable future."

David Gibbons, director for assurance at PricewaterhouseCoopers, feels that the island's longevity can be attributed to different factors.

He says: "Firstly, Bermuda has a world-renowned regulator that the business group trusts and knows that it can work with—whilst still being well respected in the global market as a regulator with integrity."

"Secondly, Bermuda has an active sector of qualified professionals that specialise in insurance. Be it underwriters via the reinsurance market, captive managers or auditors."

Gibbons also states that Bermuda's "business friendly environment"—that operates at the same pace as New York, London and Toronto—also benefits the island as clients are served at an international standard as and when they need it.

A Bermuda Monetary Authority (BMA) spokesperson adds that as the world's first captive domicile, Bermuda's core attributes are rooted in decades of experience.

Bermuda has managed to remain the largest captive domicile for more than half a century, which is no mean feat considering the increased competition from rival jurisdictions.

Bird feels that there are several reasons that Bermuda has managed to retain its powerful position for such a long time, including the growth of the island's captive infrastructure in terms of management companies, lawyers, and auditors, and also the expertise provided within that infrastructure.

"The commercial insurance and reinsurance market in Bermuda is huge with its own infrastructure, which provides a unique environment in which risk managers can benefit from holding captive meetings, market presentations and securing reinsurance for the captive."

"In addition, the regulatory framework is robust and pragmatic with a consultative approach between industry and the regulators in terms of ensuring appropriate regulations and solutions to individual challenges and opportunities."

Gibbons adds that as a veteran of the captive insurance game, Bermuda is well respected in the marketplace and existing companies domiciled on the island are comfortable with the service that they receive.

No niche required

Bermuda's rival, the Cayman Islands, has established itself as a specialist for healthcare formation, but Bird believes that Bermuda's lack of vocational calling isn't an issue.

"Our vast size in terms of captives means there is not really a niche market for captives, which we feel can limit possibilities for captive owners. It is interesting to note, however, that healthcare captives make up a significant, if not the largest, proportion of our various industry groups which own captives and we expect to see the number of healthcare captives here continue to thrive and grow as we clearly have the expertise in this area," notes Bird.

And while the island may well have marketed itself as an all-appealing location, Gibbons believes that Bermudian captives are enticed by the islands access to the reinsurance market.

He says: "We see Bermudian captives hold several different types of business, either in deductible areas or several different areas of the chain, including workers' compensation, property, marine cargo and professional indemnity."

"Bermuda also has its fair share of healthcare captive as well so I would have said it's really the access to the reinsurance market that is Bermuda's strength. Healthcare clients still come to Bermuda as opposed to the Cayman Islands as they are looking to benefit from the reinsurance market as well."

The BMA spokesperson highlights that Bermuda's experience in innovative alternative risk transfer products, such as special purpose insurers (SPIs), helps the island to not only retain its prominent position in the market but also attract new business. Bermuda's registration of 20 new insurers during the first four months of 2013 is testament to the claim.

"New registrations were driven by SPIs, as Bermuda's expertise in alternative risk transfer has made the jurisdiction a global centre for the creation, listing and servicing of insurance linked securities (ILS) that are sponsored by Bermuda-registered SPIs."

"The total volume of new ILS issued globally in 2012 was $6.4 billion, with $2.5 billion (or 40 percent) of this total being sponsored in Bermuda. Overall, SPIs have provided another option for the market to build upon Bermuda's longstanding expertise in alternative risk transfer."

Onshore versus offshore

wMarsh's recent annual benchmarking report found that in 2012 new captive owners continue to gravitate towards onshore destinations in the US and the EU. But according to the BMA spokesperson, the statistics aren't a cause for concern for Bermuda.

"Clearly the environment overall is becomingly increasingly competitive. However, Bermuda is in the unique position of being able to service the full spectrum of insurance: from commercial insurers, to captives to reinsurers. The entire jurisdiction remains committed to providing quality regulation and service delivery for captives. This commitment is driven by the recognition that captives remain a core business for this jurisdiction."

Gibbons is of the opinion that companies are subject to individual business cycles, so in mature markets such as Bermuda clients tend to come and go.

"I think that in any market people are looking at what makes the most sense for them, and are therefore basing their decision of where their business should be located on facts."

"There are also uncertainties surrounding other issues in the market such as US taxation and Solvency II. Captives come to Bermuda because they think it's the best place with regards to Solvency II as it allows them the option of either being Solvency II equivalent or not."

Bird feels that the reference to onshore versus offshore "is moot these days and frankly, misleading".

"Where a successful model exists in a country, so other jurisdictions are bound to copy it and there are many captive domiciles in a variety of territories. It is to be expected that new captive owners will sometimes set up elsewhere."

"The differences, where they exist at all, are often negligible and certainly, what you can do in US domiciles for example, you can virtually always do in Bermuda as well. So, as long as new captive owners are properly informed, Bermuda will continue to grow," adds Bird.

Committing to the cause

In April, the Bermuda Business Development Corporation (BBDC) completed its merger with Business Bermuda and the Insurance Development Council.

The BMA spokesperson says that the BBDC merger has renewed the island's focus on the development of new business, as well as supporting existing business.

As a member of one of the BBDC sub-committees, Gibbons has first-hand experience of the recent merger. He feels that by setting aside competitive differences, the service professionals involved have been able to work towards the betterment of the territory.

"We've realised that its good for all of us to promote Bermuda, and talk about Bermuda's strengths, rather than us being competitive in the same space, so I think the merger has been a very positive event."

"There is a lot more competition out there for Bermuda, as a lot more US states are entering the game. So Bermuda's continued success is incumbent on the BBDC and everyone in the Bermuda market to continue to talk about the advantages of Bermuda." CIT

Important milestones for Bermuda's captive sector

- **1950's**—The 'father' of captive insurance, Fred Reiss, forms Steel Insurance Co of America for Youngstown Sheet & Tube Co, Ohio—the name 'captive' is born.
- **1958**—Fred Reiss forms American Risk Management.
- **1962**—Fred Reiss forms International Risk Management, incorporated in Bermuda by special act of parliament. Bermuda's captive movement begins in earnest.
- **1965**—Alexander & Alexander become first major brokerage subsidiary to set up in Bermuda. Hurricane Betsy hits US Southern States. Worldwide reinsurance market develops.
- **1968**—Ford Motor Company chooses Bermuda for own captive, Trans-Global.
- **1969**—BMA established. Two protection and indemnity clubs established by private charter in Bermuda.
- **1974**—Between 350 to 400 captives reported in Bermuda.
- **1977**—Major influx of reinsurance captives. Seven hundred and fifty insurance companies registered.
- **1978**—Insurance Act 1978.
- **1980**—Insurance Accounts Regulations 1980 and Insurance Returns & Solvency Regulations 1980.
- **1981**—Companies Act 1981.
- **1984/6**—Hard excess liability market. ACE & XL formed to increase capacity for third-party liability coverage.
- **1988**—Fred Reiss—now 62-years-old—sells Bermuda-based Reiss Group to Swiss Re. Bermuda signs tax convention with US.
- **1992/3**—Hurricane Andrew. Growth in new formations and acquisitions in Bermuda provides additional property/catastrophe capacity. Partner Re and Renaissance Re founded in Bermuda.
- **1995**—Bermuda Insurer Classification System introduced.
- **2000**—Segregated Accounts Company Act 2000.
- **2001**—Following 9/11, Bermuda market provides more insurance and reinsurance capacity. New formations include Axis, AWAC and Endurance.
- **2002**—BMA takes on insurance supervision from Bermuda Government's Ministry of Finance to becomes Bermuda's independent, integrated financial services regulator.
- **2005/6**—Formations post-Hurricanes Katrina, Wilma and Rita, provide another wave of start-up companies—including Lancashire and Hiscox. Growth of sidecars.
- **2008**—Special Purpose Insurer Legislation facilitates subsequent growth of Bermuda as leading centre for cat bonds/insurance linked securities (ILS).
- **2010**—Bermuda's captive market writes more than $21 billion in gross written premiums.
- **2011**—Bermuda achieves broad equivalence with Solvency II for commercial insurers and subsequently confirms that Bermuda will not apply Solvency II-type regime to captives.
- **2012**—The market capitalisation of ILS issued during 2012 increased to $6.4 billion, with Bermuda increasingly becoming a global centre for the creation, listing and servicing of ILSs that are sponsored by SPIs.

Source: Bermuda Monetary Authority

In a perfect world

CIT's experts reveal what they like to see in a regulator, with Bermuda's and Vermont's coming under the microscope

What attributes would your ideal captive regulator have, and how are the regulators in the jurisdictions in which you work measuring up?

Thomas McMahon
President
Cedar Management Limited

After decades as the world's leading captive domicile, in 2013, Bermuda is still maintaining that position and will undoubtedly do so for many years to come. There are many reasons why Bermuda has been able to achieve this dominant position, none more important than the intelligent, efficient and effective regulatory regime that has been applied to the captive insurance sector, which has evolved over those same decades to the risk-based approached that is in place today.

One would expect any insurance regulator to possess a minimum set of attributes such as basic insurance knowledge, be competent and efficient, and have access to key support staff. However, when dealing with the captive sector, a regulator should possess certain attributes that are in addition to what I would refer to as the basic attributes listed above. This is of key importance when the market that is being regulated is not just a captive market, but includes a commercial market—such as Bermuda. It is in the possession and utilisation of these additional attributes that captive regulators should be measured:

- A captive regulator must possess a solid understanding of what a captive insurance company actually is, coupled with a solid appreciation of risk-based regulation. A captive insurance company is not a commercial insurance company and should not be regulated as if it were one. Using its knowledge base of the purpose and role of a captive in an organisation's risk management function, and recognising the distinction between it and a commercial insurance/reinsurance company, the Bermuda Monetary Authority (BMA) has been able to put in place a class system of licencing that results in a layered level of regulation depending on the level of unrelated business written in the company. This is risk-based regulation in its finest form.This risk based-/class of licence-based regulatory framework has enabled the BMA to present a strong and credible argument for the bifurcation of the Bermuda insurance market for Solvency II equivalency, with equivalency just being sought for the commercial sector of the market.
- A captive regulator should be guided by the principle of proportionality in the development and enforcement of regulations. This attribute is key to the successful adoption of risk-based regulation and formed the basis for the levels of regulation applied to the various insurance licences classes in Bermuda. In addition, the BMA, in its Insurance Code of Conduct, published in 2010, clearly stated that they would assess compliance with the code in a proportionate manner relative to the nature, scale and complexity of the regulated entity. Clearly these first two attributes were key to the successful development of the regulatory environment for the Bermuda insurance market and its many sectors.
- A captive regulator should be willing to consult with and listen to the industry that it is regulating. Bermuda can take pride in the excellent consultative processes that have been in place for many years between the industry, the Bermuda Government and the BMA. And I am pleased to say that in Bermuda it is indeed a two-way street. The industry has always been included in the consultative process when amendments to regulation have emanated from the BMA and/or the Bermuda government. The BMA and the government have also been receptive to many regulatory changes and/or enhancements suggested by the industry.
- A captive regulator should be approachable. The BMA has always encouraged and been available for dialogue with

regulated entities should any regulatory issues arise. In addition, the BMA also encouraged 'meet and greet' meetings with new, potential and even existing clients. This has proven to be of tremendous value in the development of a long-term relationship between the client and Bermuda.

There is no doubt that the insurance regulatory framework in Bermuda works very well for the complexities of the Bermuda market. It is flexible yet effective, is in compliance with international standards and is proactive with change to suit changing market conditions. The BMA have been able to achieve its success in this area through its investment in personal and IT systems. Proof of the BMA's success as a regulator is the level of esteem and respect that is held internationally and the level of input accepted from Bermuda in setting international standards.

Karl-Ove Andersson
Senior vice president
Marsh Management Services

The new realities of risk demand more from risk management than ever before. Working closely with the regulators in every domicile in which Marsh operates is key to meeting the demands our clients face on the part of stakeholders, trading partners, and ratings agencies for formal enterprise-wide governance.

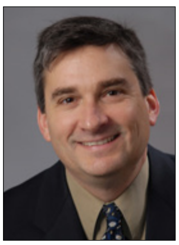
A considerable amount of time and cost goes into developing a business plan. Most regulators appreciate that and ensure licences are issued quickly. They recognise that commercial organisations are looking for ways to improve their financing arrangements. Given ongoing challenging economic conditions, many owners are using their captive vehicles to facilitate achieving such goals. In implementing new standards for captive reporting, regulators keep members of the captive industry informed and will often ask for feedback on how changes can be made. Early discussion around licences, expansion of licences, the set up of the organisational structure and other topics helps to simplify the application phase and can reduce costs for captive owners. Open communication with regulators is essential to quickly and easily solving issues as they arise.

In the US, growth in the number of captives and domiciles can pose challenges for regulators in striking the right balance between traditional regulatory techniques and commercial awareness. Many are now looking to hire industry professionals as a way to complete their supervisory teams. Many of the more established domiciles have created distinct captive units within their insurance departments. Emerging domiciles continue to make use of the best working practices, methods, and legislation from more established domiciles. Many domiciles are proactive with their legislative and regulatory approach to captives, creating new laws or revising existing ones in order to keep pace with industry changes.

The Solvency II Directive remains a key challenge for EU regulators. In preparation for the demands that Solvency II will place on supervisory teams, many regulators have added to their staff. Similar to their US counterparts, EU regulators have been hiring personnel from the commercial insurance industry to keep pace with developments. The regulators have been open-minded in ensuring that our captive owners understand the rules, procedures, and requirements for Solvency II. For example, one even recently assigned an individual to act as a kind of 'client executive' to walk a non-European organisation through the process.

Regulators in offshore domiciles continue to attract captive owners with their practical, proportionate, and risk-based assessment of new applications. These domiciles are also known for their ability to react quickly to enhance or develop legislation as market demands change in order to ensure competitiveness for captive owners. As companies continue to grow through acquisition, corporate ownership can change and, globally, re-domiciliation legislation makes moving captives between domiciles easier. Many regulators have seen an increase in activity in this area.

At Marsh, we continuously work on our relationship with the regulators in each domicile. Collaboration based on knowledge, experience, and a commitment to a well organised and functional captive market is the best way to meet the evolving needs of the industry.



Richard Smith
President
Vermont Captive Insurance Association

One of the key elements of any captive domicile in the industry is the strength of its captive regulators. Most domiciles, at least in the US, have very similar captive laws (even copying mistakes from other domiciles' statutes) and regulations. How those laws and regulations are interpreted and carried out by the regulators is what divides a good captive domicile from all the rest.

A captive is part of a long-term risk management solution. Captive owners need regulators and a jurisdiction that will be a partner in their success. As needs change, captive owners need a domicile that offers support, strength and resources to be there for them. Vermont has a great track record. We have resources allocated to support this industry. Vermont has been in the captive industry since the early 1980s and the longevity, expertise and support that the state has built up around this industry has created what people consider the 'gold standard' in terms of the regulatory environment.

Every year, Vermont regulators and the captive private sector look for ways to improve Vermont's captive statutes and regulations. It's a very innovative and changing industry and if you're not looking at ways to keep current, or be on the leading edge in terms of regulation and statutes, then you start falling behind as a domicile. Flexibility is important, particularly in a dynamic area such as captive insurance. Innovation and continued collaboration between the regulators and private sector to ensure that legislation keeps up with market needs is imperative. Vermont is very skilled at keeping things current in this way.

Another important factor in selecting a domicile is the captive insurance industry's clout in the domicile. In Vermont, it's both the strength of the regulatory team and the solid support of the political leadership that provide that clout. It doesn't matter which party the political leadership is from; there is a consistent commitment of government at all levels that is key in how well the regulatory branch operates.

A regulator's clout also makes a difference to those outside the domicile. The captive insurance industry is facing multiple threats from national and international regulatory bodies focused from financial solvency to governance. The issue is the insurance industry, including captives, has actually provided a bulwark that strengthened the economy during these tough times, and it is incumbent on the industry and regulators to work with each other to better understand this issue and promulgate appropriate efforts if needed. In Washington DC, the Vermont captive regulatory team is the most respected in the US and therefore able to review any regulations proposed for the industry, while pushing back on regulatory overreach. At the end of the day, domiciles with good regulation often already institute these standards because they make sense. Vermont regulators have clout, and that's a big plus for the whole captive industry.

The regulatory environment in the State of Vermont is proactive and responsive. Our captive licensing process and captive laws are kept up-to-date to better meet captive insurance needs. With the support of our state government, our captive laws are able to adapt as the industry evolves. The importance of captive regulators to the industry cannot be overstated. CIT

Bermuda: front and centre

Keeping a sharp focus on the key elements of the relationship between the client and the fronting carrier is critical to the success and longevity of that relationship, says Stuart Hayes of AIG Global Risk Solutions

Based on our experience, we believe the defining elements of a multinational captive fronting programme have remained consistent over the last several decades:

- Security
- Programme structure and underwriting
- Global reach and regional compliance
- Administration.

Security: both parties to the relationship need assurance that the programme will respond as intended and designed. Security falls into four areas: the financial strength of the captive and its parent; the captive's retrocession programme; reinsurance agreements and other credit mitigating instruments; and the concurrency between the captive's retrocessional wordings and the front-end policy wordings to eliminate gaps in cover and timing of risk.

Programme structure and underwriting: traditionally, fronting programmes facilitate local policy issuance and reinsurance as part of an overall strategy of risk retention, either in whole or in part, by our clients. Designing a programme structure to efficiently meet the client's objectives is critical to a programme's success. Risk managers value a fronting partner's ability to: provide expertise in analysing complex and unique risks; structure innovative and efficient captive programmes targeted to their specific needs; insure virtually any lines of business; and provide access to significant risk-bearing and risk financing capacity.

Global reach and regional compliance: multinational expansion has resulted in companies needing to address risks across wider geographic areas, each with their own regulatory requirements. Companies operating in emerging economies face even greater uncertainty since these countries do not always have well established or documented insurance regulation and are increasingly issuing new regulations and oversight requirements. Risk managers look to their global fronting partners to invest the substantial time and resources necessary to navigate the challenges of conducting business worldwide, while operating as efficiently as possible in a global environment of increased regulation and regulatory scrutiny.

Administration: effective administration remains a key criterion for risk managers when choosing a fronting partner. Three critical elements determine administrative strength: global servicing capacity, centralised administration and IT systems, and expeditious cash flow. The last element has become increasingly important as improvements enabling more efficient tracking and movement of cash flows facilitate captives' building net worth, paying claims and complying with premium payment warranties on retrocession programs as well as reducing foreign exchange risk.

A fronting provider will seek to utilise its available network of owned operations, supported wherever required by local insurance partners. The goal, as a sustainable service provider, is to generate fee income by leveraging the network and providing a valuable service to clients without eroding the fronting carrier's capital base as part of the captive fronting programmes provided. Fronting carriers are acutely aware of the impact on their regulatory capital requirements, and the fact that many country regulators will often not recognise reinsurance provided by unauthorised reinsurers. Territories where these requirements can be burdensome include the US, Canada and Australia. For example, in the US, the vast majority of captives are considered unauthorised reinsurers. In these circumstances, the four factors that combine to negatively impact a fronting carrier's capital are:

- Outstanding loss reserves
- Incurred but not reported claims
- Unearned premium
- Loss payables.

The fronting carrier may require collateral to offset the negative impact to the carrier's capital as a result of their inability to take credit for the reinsurance provided by the captive reinsurer. The collateral provided will preserve the fronting carrier's capital and also mitigates credit exposure to the captive/client.

Increased global regulation creates the need for local expertise within a global programme, a need that can be well served by fronting carriers with an extensive global network. The lack of centrally available, reliable information contributes to captive uncertainty in directly transacting business in some jurisdictions for fear of falling foul of local regulations. A fronting carrier's locally licensed operation provides value to the relationship between captive and fronting carrier, as it can be challenging and costly for captives to keep pace with the various territorial regulatory changes.

If the fronting carrier's service does not meet the captive's expectations, the risk is that the captive performs the function itself. As sophisticated risk financing vehicles with considerable individual net worth, many captives have conducted feasibility studies looking at the option of licensing themselves in those territories where their largest exposures, and consequently their largest premiums, are located. This research provides captives with an understanding of the challenges that fronting carriers face and enables them to better evaluate the service provided. Notwithstanding that the uncertainty in directly transacting business in unfamiliar jurisdictions often impacts the decision making process, proceeding without a fronting carrier prevents the local insured from benefitting from a local insurer's services, and the captive from realising economies of scale provided by a fronting carrier's centralised network.

Keeping a sharp focus on the key elements of the relationship between the client and the fronting carrier is critical to the success and longevity of that relationship, and must always remain front and centre in order for the relationship to thrive. CIT

Stuart Hayes
Vice president and client relationship manager
AIG Global Risk Solutions

Big friendly RRG

Michael Rogers of Risk Services Companies tells CIT why the group captive structure can be a winner, and how companies should go about setting one up

JENNA JONES REPORTS

Why do your clients decide to form an RRG?

Our clients desire to form a risk retention group (RRG) largely reflects the common diversity of reasons for forming a group captive generally. A RRG unlike most other captives acts as a direct writing insurance company, rather than a reinsurance company, and therefore eliminates the reliance of the traditional insurance market to provide fronted paper and enables the client to control its own destiny. With the direct writing capabilities comes the ability to access the reinsurance market and unbundle underwriting, claims, loss control and management to the best of breed service providers that specialise in these areas.

Sometimes, decision comes from a perception that the traditional insurance market is miss-pricing the exposure. For instance, we have one RRG client that had a pre-existing programme insured by a traditional insurer that had an extraordinary loss ratio of under 10 percent, which simply was not reflected in the premium charged. This programme also required unique underwriting and claims handling, which the traditional insurer could not or would not provide.

In other cases, the traditional insurance market is unwilling or unable to provide the coverage needed. An example is a client that had a manufacturing liability programme requiring an endorsement that the traditional insurance market would simply not provide. The RRG so formed did provide the endorsement, and ironically the traditional insurance market, buoyed by the RRG's success, began to offer the endorsement to its traditional policyholders.

The bottom line is that the decision to form a RRG, with the unique benefits afforded by the structure, largely mirrors that for group captive formation generally. This includes: insurance availability and affordability; unique coverage and policy forms that are not generally available from traditional insurers; access to the reinsurance market; utilisation of claims handling; risk management; underwriting procedures that are not afforded by traditional insurers; and a group programme having better loss experience than the industry class as a whole.

Why did they choose an RRG over a traditional captive?

Pursuant to the US Federal Liability Risk Retention Act (LRRA) under which RRGs are formed, there are invaluable preemptions afforded to RRGs that are not available to non-RRG captives or traditional insurers.

First and foremost, it is important to recognise that multi-state unauthorised insurer laws make it difficult for a group captive having a significant number of policyholders to operate on a multi-state basis without using a fronting insurer. Direct procurement statutes require virtually all aspects of a captive operation, including any communication with the policyholder, whether by mail, email, telephone, or other methods of communication to take place solely within the captive's domicile and not interstate. Otherwise, the captive can be deemed to be doing an unauthorised insurance business in the domiciles of its policyholders and be subject to significant penalty.

The use of a fronting insurer to comply with multi-state licensing requirements carries with it significant drawbacks. One is obviously the often-significant fronting fee involved, along with dependence on the front for the captive to operate and the related year-on-year collateral requirements of such fronting carriers. Moreover, the captive can very often be limited to the policy forms and rates that the fronting insurer has on file in other states—thereby minimising or obviating the form and rate flexibility that captives should offer to its policyholders.

Under the LRRA, RRGs can largely do business on a multi-state basis without the cost and drawbacks of having to use a front. Under the LRRA, a RRG is licensed only in the state of domicile and can do business on a multi-state basis by a filing registration in the non-domiciliary states in which it seeks to do business. Moreover, policy form and rate approval is required only by the RRG's domiciliary licensing state. Non-domiciliary states are preempted from imposing rate and form approval on RRGs. Thus, the RRG can freely operate on a multi-state basis without the use of a front and utilising the policy form and rate approved by its domiciliary state.

Moreover, under the LRRA, RRGs for the most part are preempted from financial responsibility requirements that would require the use of only insurers licensed in a policyholder's state. This feature is particularly useful when dealing with commercial auto financial responsibility requirements, but it has also been advantageous to RRGs' providing professional medical liability, and in many other situations, such as for warranty administrators.

Another often under-appreciated advantage of RRGs is the ability to secure capitalisation for captive formation from potential member/policyholders without US Securities and Exchange Commission/federal securities filings and related state blue-sky law securities filings. While hastening to add that organisers are still subject to anti-fraud provisions of these state and federal securities laws, the legal expense, time, and labour obviated in not having to make such filings in order to raise capital for the RRG's funding, are enormous.

What advice would you give to a company interested in setting up its own RRG?

In considering the formation of a RRG, it is important that the proposed group clearly defines the goals and objectives of the RRG programme, and works closely with its selected service providers to ensure that the RRG's filed business plan addresses those goals and objectives. It is also critical for the RRG to select service providers that have RRG experience. A RRG is a unique entity, which, although often licensed as a captive insurance company, acts very much like a traditional carrier and as such requires strong expertise dealing with both domiciliary and other states regulators.

Additionally, it is important that the proposed group understands that the formation of a RRG is to provide a long-term solution to its liability insurance needs and as such requires a long-term commitment from the proposed members.

What must affinity groups consider before opting for the RRG structure?

For any affinity group that's considering forming a RRG, we suggest these guidelines:

- Go with a pro—getting an RRG off the ground successfully is not a do-it-yourself project. Any group considering the RRG business model faces a complex task that includes developing the corporate documents, capital contributions, preliminary marketing, board development, selecting state of domicile, licensing, and registering the RRG in other states where it plans to do business.
- Due diligence essential—the track record of any captive manager being considered should be checked. How many RRGs has the organisation launched? How many are under management? Talk with the manager's clients.
- Flexibility to meet your needs—is the group seeking total management: the full range of services including administration, underwriting, claims and risk management, reinsurance, regulatory compliance, and marketing? Or does it have existing relationships that provide some of these functions. The group should select a captive manager that can tailor services to specific requirements.
- Specialist best qualified—we believe that RRGs are best served by managers whose primary business is RRG administration and have the professional staff to provide the full range of services.
- Governance—the success of any RRG depends on strong board leadership. We recommend a blended board with the majority of directors coming from the insured industry, supplemented by insurance professionals.
- Reinsurance—most RRGs require reinsurance to protect against severe losses, and a few buy quota share reinsurance to enable growth. Reinsurance should be purchased from reinsurers with a minimum "A-" rating from A.M. Best.
- State of domicile—we tell our clients that the best domicile is the one that expedites the initial licensing application for admission and, once licensed, treats its captives fairly and has a good relationship with its captive manager. We advise clients generally against choosing the state where its operations are based as the state of domicile. CIT

Go with a pro—getting an RRG off the ground successfully is not a do-it-yourself project. Any group considering the RRG business model faces a complex task

Michael Rogers
Chairman and CEO
Risk Services Companies

All hands in check

Why are some US states still wary of the RRG structure? CIT investigates

JENNA JONES REPORTS

US Congress passed the Product Liability Risk Retention Act in 1981 to allow risk retention groups (RRGs)—a new type of insurance vehicle—to cover product liability exposures.

In 1986, Congress expanded the act to include commercial liability, renaming it the Liabilty Risk Retention Act (LRRA).

As Douglas Powell, senior financial analyst at Demotech explains, the need for RRGs arose when property and casualty insurer appetites for underwriting certain liability exposures began to tighten.

"[The] LRRA was signed into law in the US to provide a mechanism for the placement of liability insurance coverage and created a new form of insurance carrier, an RRG."

The National Risk Retention Association (NRRA)—a non-profit trade group—was formed to protect the rights of its RRG members. Its website states that: "The Liability Risk Retention Act is a federal statute which is not overseen or regulated by any federal agency. The primary regulatory authority for a risk retention group is its state of domicile. Other states have regulatory authority curtailed by federal law."

Chairman of the NRRA, Sanford Elsass, says: "The primary mission of NRRA is to defend the right of RRGs to operate free of most regulation in states other than their home state. RRGs were authorised by federal law—the LRRA—to write liability insurance throughout the US, so long as they are duly licensed and regulated in a single state."

But Burke Coleman, general counsel and compliance manager at Demotech, explains: "While states generally have the power and duty to regulate the business of insurance, the LRRA exempts RRGs from much of the state regulation outside their home state."

"Many non-domiciliary states are wary of RRGs because they cannot exercise the same regulatory authority that they have over other carriers operating in their jurisdiction."

Elsass says that regulators in some US states believe that RRGs are a threat to state regulation, so they attempt to impose illegal fees, registration requirements, and other burdens that make it tough for RRGs to do business in their states.

He says: "Most RRGs are small companies with limited resources to assert their rights under the federal law. That's when the NRRA gets involved. Our association is vigilant in monitoring threats to RRG operating authority and has headed off harmful actions by explaining the federal law to state and local entities that try to interfere with the legal operation of RRGs."

"NRRA has won landmark cases in the federal courts and sponsored legislation to create an enforcement mechanism in the LRRA, so RRGs would not always have to go to court to assert their rights."

While progress is being made to restrain biased regulatory treatment being placed on RRGs, there is still a way to travel before all non-domiciliary states adhere to the law.

Earlier this year, the US Court of Appeals for the Ninth Circuit supported a district court ruling in Nevada to allow RRGs the right to do business in the state.

In their decision, the judges said: "The LRRA broadly preempts 'any state law, rule, regulation or order to the extent that such law, rule regulation or order would … make unlawful; or regulate, directly or indirectly the operation of a risk retention group'."

Liability limitations

Unlike the majority of alternative risk transfer vehicles, RRGs are limited in that they can only write liability coverage. And while some people would see the restriction as a significant drawback, Robert Warren, client services manager at Demotech, explains that catering to a niche market was intentional.

He says: "The inability of professional service providers, public service representatives as well as other commercial and business ventures to access affordable, adequate liability coverage was the catalyst for the passage of the LRRA."

"The availability and capacity for property coverage was not a part of the legislative initiative as adequate property insurance capacity has been available through the private market or public FAIR (fair access to insurance requirements) plans."

Equally important as coverage limitations, according to Powell, is that in order to be an insured of an RRG, the insured must be an investor/shareholder of the group.

He says that as coverage options are restricted, RRGs tend to insure medical providers, product manufacturers, law enforcement officials and contractors. At the end of 2012, medical professional liability RRGs accounted for more than 50 percent of the RRG marketplace in terms of direct premium written.

Powell says: "RRGs are viewed as an enticing alternative to traditional insurance by some doctors willing to join together for their liability insurance, due to a section of the Affordable Healthcare Act offering incentives for healthcare providers to become part of 'accountable care organisations'."

Unlike traditional captive insurance companies that generally focus on a single parent structure, RRGs "are incorporated by numerous like-minded businesses with a specific industry," says Powell.

Joseph Petrelli, president of Demotech, says: "RRGs offer liability insurance protection to those within a specific industry facing availability or affordability crises. Having multiple owners/members with similar liability coverage needs often leads to benefits from risk pooling, participation and experience sharing by members."

State of control

Elsass feels that the increase in US states adopting captive insurance laws could help the situation.

He says: "As more states enact captive laws, they will hopefully develop professional staffs that understand the benefits and facilitate the operation of the captive industry and its various segments including risk retention groups. Today, more than 30 states have captive laws and we anticipate more."

"While many states welcome the financial benefits of having such laws, they will be challenged to meet the high standards set by the 'domicile' states, such as Vermont and Hawaii, that have pioneered captive regulation over the years."

But whatever may happen, Elsass says that the NRRA will continue to defend RRGs in the federal courts. "We'll advocate for the industry in congress, state legislatures and even before the National Association of Insurance Commissioners."

"NRRA is also expanding its educational role through our annual conference and member communications. Our members belong to NRRA because they know the association has the resources to support them when they come up against a powerful state." CIT

2013

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Bermuda Captive Conference 2013

Location: Bermuda
Date: 9-12 June
www.bermudacaptive.bm

Catch up to Bermuda, the global force and master innovator in the captive market. Listen to industry specialists, network with other captive owners and join in discussions on hot topics and how they will shape the future of this industry. The Bermuda Monetary Authority will also be available throughout the conference to answer any regulatory questions.

Airmic Conference 2013

Location: Brighton
Date: 10-12 June 2013
www.airmicconference2013.com

The Airmic Conference 2013 will open its doors to over 800 UK industry buyers and sellers of the insurance market seeking to keep up-to-date with trends, discover new service providers, learn and network with their peers, and be inspired by our keynote speakers.

Western Region Captive Insurance Conference

Location: Arizona
Date: 10-12 June 2013
www.westerncaptiveconference.org

The Western Region Captive Insurance Conference is the perfect source to gain understanding by interactions with the regulators from Arizona, Missouri and Utah, experts from all segments of the captive industry and owners and managers of captives and RRGs. The conference caters to those who are both new and old to the captive industry detailing what works and what is important to the industry. Join us as an attendee, session speaker or exhibitor!

VCIA Conference 2013

Location: Vermont
Date: 13-15 August 2013
www.vcia.com/annualconference/

The conference will feature nearly 60 panelists, many of whom are captive owners, sharing case studies and personal experience. Tons of education and great opportunities to mix and mingle with all the key players in the industry; all in beautiful Burlington.

The VCIA Conference is a great choice for any level of industry professional--from the newcomer to the seasoned professional.

Industry appointments

Michael Halsband and Deanne Nixon have been named as the joint leaders of Sirius International Group's new insurance linked securities (ILS) team.

Bermuda-based Sirius Group is the reinsurance unit of White Mountains Insurance Group.

Halsband joins Sirius Group from Deutsche Bank where he led the firm's property and casualty insurance solutions practice. He will be based in New York and report to Allan Waters, president and CEO of Sirius Group.

Nixon joined Sirius Group in 2003 and most recently held the role of senior vice president for Sirius International Insurance Corporation's Bermuda branch. She will be based in Bermuda and also report to Waters.

Waters said: "Capital markets participation in the property catastrophe risk arena is growing rapidly, changing the face of what has historically been one of the most profitable sectors in the traditional reinsurance business."

"This strategic initiative leverages White Mountains' and Sirius Group's extensive successes in both capital markets executions and property casualty underwriting. The Sirius ILS team will provide their deeply knowledgeable experience and wisdom to our current and new partners who wish to access this rapidly developing market."

American International Group (AIG) has named Anthony Philip as president and CEO of American International Company in Bermuda.

Philip will replace David Valzania, who has recently been named head of global risk solutions for the US and Canada.

In his new role, Philip will oversee regulatory matters and act as AIG's principal liaison with the Bermuda Monetary Authority (BMA). He will also serve on the boards of the American International Reinsurance Company and American International Overseas.

Philip joined AIG in 2008 as senior vice president and general counsel for AIG in Bermuda.

Prior to joining AIG, he was a part of the senior management team of Flagstone Reinsurance and West End Capital Management.

Rob Schimek, president and CEO of AIG for the Americas region, said: "We are very pleased to have Philip leading our operations in the country."

"He brings a wealth of knowledge about the business and regulatory environment in Bermuda through his background in corporate law and previous experience working at the BMA."

Marsh has appointed Neil Irwin to lead the firm's business development across the Middle East and North Africa (MENA).

Irwin will be based in Dubai and report to Robert Makhoul, CEO of Marsh MENA.

Irwin joined Marsh in 1991 and has held a number of strategic business development, consulting and senior management positions. He most recently held the role of managing director responsible for Marsh's business development across Europe.

Makhoul said: "Marsh is committed to offering the full spectrum of specialist risk management, employee benefit and insurance solutions that our clients in this dynamic region require."

"Irwin is familiar with our region and this combined with his extensive global experience, will prove a very powerful force in supporting the delivery of Marsh's promise to its clients across MENA."

Irwin added: "Expanding the value Marsh delivers to our clients is fundamental to the firm's continued success in MENA. I very much look forward to working with our senior management team and industry experts to develop solutions that will continue to contribute to our clients' future prosperity."

Nelson Mullins Riley & Scarborough LLP has recruited attorneys Kevin Doherty and Cynthia Wiel to its Nashville office.

Doherty has joined the firm as a partner and will practice in the area of insurance regulatory law, with particular emphasis on captives, risk retention groups (RRGs), self-insurance funds, and other alternative risk vehicles.

In 2011, Doherty helped to rewrite the captive insurance law in Tennessee that allows the state to more aggressively attract captives and RRGs.

Docherty is chairman and president of the Tennessee Captive Insurance Association (TCIA).

Wiel, who will also practice in the captive area, joins the firm as of counsel. Wiel will concentrate on insurance regulatory, business, healthcare, and municipal utility law.

Wiel serves as the co-chair on the government relations committee for the TCIA.

"We welcome Doherty and Wiel to the firm and to our Nashville team and look forward to introducing them to our clients," said Larry Papel, Nelson Mullins's Nashville office managing partner. "Their experience adds to the firm's regulatory and healthcare practices and provides depth to our scope of client services."

Towers Watson has named Michael Murphy as managing director of its risk consulting and software (RCS) business in Europe, the Middle East and Africa.

The firm's RCS business provides actuarial, strategic, performance improvement, financial, and software solutions and advice to life assurers, insurers, and reinsurers globally.

Murphy joined Towers Watson in 2011 to lead the RCS operations in Continental Europe, Ireland and South Africa. He previously held the role of managing director of Aviva Insurance Southeast Europe.

Rory O'Brien, global leader of Towers Watson's RCS business, said: "Murphy combines a deep knowledge of our business with valuable insights gained from his experience in local and regional leadership roles with insurers. He will add a valuable perspective to our global and regional management teams as we aim to support clients through the various market changes taking place across the EMEA region." CIT

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