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NCDOI names new captive director

Debbie Walker has been appointed director of captive insurance at the North Carolina Department of Insurance (NCDOI).

As head of the department's captive insurance section, Walker will be responsible for analysing captive insurance licence applications and overseeing the ongoing regulation of licensed captive insurers in North Carolina.

Wayne Goodwin, the state's insurance commissioner, said: "I can think of no one better equipped to take on the exciting challenge of growing the captive insurance market in North Carolina. In addition to a wealth of professional experience, Debbie Walker brings an exceptional level of customer service to this position."

Walker, a certified public accountant, has worked in financial regulation at the department for more than 20 years and was named chief financial analyst in 2006. Prior to joining NCDOI, she held various accounting roles in the private insurance industry.

Walker said: "I am enthusiastic about my new role as director of captive insurance, and I look forward to working with captive managers, captive insurers and other captive service providers. It is my goal and the department's goal to make North Carolina a respected and leading captive domicile. I feel confident that, with our sensible pro-business approach to regulation and our responsive and knowledgeable staff, we will be successful."

Walker's appointment swiftly followed news that NCDOI had issued four captive insurance company licences since the state's legislation was enacted in October 2013.

They are West & Joyce, Cade Reassurance and SR Insurance, which are managed by Atlas Insurance Management in North Carolina, and Synergy Insurance, which is managed by Synergy Captive Strategies in Las Vegas.

Goodwin said: "North Carolina is off to a strong and promising start as a captive domicile. With our state-of-the-art law and commitment to the success of captives,

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Captives could be swept up in federal vortex, warns Fitch

The US government is becoming increasingly interested in the captive insurance market niche, an area currently regulated at the state level with little federal involvement, according to Fitch Ratings.

The rating agency said that a form of captive insurance used to finance conservative statutory reserve requirements for some products sold by life insurers has piqued the interest of two agencies of the Federal government—and that most insurance has historically been regulated by states.

A Federal Insurance Office (FIO) report on 12 December 2013 included recommendations on captive reinsurers. On 29 December 2013, it was reported that the SEC had asked at least five publicly traded life insurers for information on their use of captive reinsurance.

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HK promises to change captive's underused status in Asia

Hong Kong has been making a recent, concerted push to develop its status as a captive domicile.

As well as a bill aiming to slash the tax on captive profits by half, with help from the Inland Revenue, the government and the Hong Kong Federation of Insurers held a workshop on captive at the Asian Financial Forum on 14 January.

Speaking at the workshop, the permanent secretary for financial services and the treasury, Au King-chi, said: "The government has renewed its efforts to broaden Hong Kong's insurance market."

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NCDOI names new captive director

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I am confident we will become one of the most desirable states in the country for the formation and re-domestication of captive insurers."

North Carolina signed its Captive Insurance Act into law on 19 June 2013. At a captive seminar in December 2013, Goodwin expressed his appreciation to the North Carolina Captive Insurance Association for its efforts to draw business to North Carolina and his optimism about the future of captive insurance in the state.

Goodwin said: "North Carolina has a law that makes us competitive with the most successful captive domiciles in operation. We will use a consistent and sensible approach to regulation, always remaining responsive to the needs of the captive industry."

Atlas was licensed as a captive insurance manager in North Carolina in December 2013.

Speaking at the time, Martin Eveleigh, chairman of Atlas, said: "Captives domiciled in North Carolina will benefit from reasonable capital requirements and competitive premium tax rates."

"Importantly, the regulatory team at the North Carolina Department of Insurance has already demonstrated its commitment to being flexible and business-friendly."

Captives could be swept up in federal vortex, warns Fitch

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This heightened federal interest may stem from a New York State Department of Financial Services report in June 2013 that criticised life insurers' use of captive reinsurance, said Fitch.

"The FIO's recommendation, as per their report, appears to encompass all captive reinsurers. Although it was reported that the SEC (Securities Exchange and Comission) requested information only from a group of public life insurers and the FIO's discussion centered on life insurers' use of captives, the FIO's intent remains unclear as the wording chosen for that section of their report may have been simply general in nature."

While federal interest currently centres on life reinsurance captives (ie, captives sponsored by life insurers) and not traditional single parent or group captives formed by industrial corporates, Fitch said that traditional captive insurance could be swept up in the vortex if some regulators and others do not appreciate the difference between the two types of entities.

This could create the possibility that 'captive reinsurers' will become simply 'captive insurers', giving rise to mission creep as the regulatory process evolves.

The National Association of Insurance Commissioners has several current initiatives related to life insurers' use of captive reinsurers. An NAIC working group is addressing the subject and has already published a whitepaper.

"Some of these initiatives have been quite controversial and several state regulators have expressed distinctly different opinions regarding the best direction of the NAIC's efforts and the appropriateness of using captives to reinsure life insurance," added Fitch.

"In the extreme, subjecting traditional captive insurers to new reporting requirements or other new regulation would add cost and complexity to the captive insurance process and may ultimately result in non-insurance sponsors deciding not to form new captive insurers and possibly even to wind up existing captive insurers."

HK promises to change captive's underused status in Asia

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"In particular, we are introducing measures to promote Hong Kong as a domicile of captive insurers."

"To this end, we are delighted that the central people's government is encouraging mainland enterprises to set up captives in Hong Kong so as to enhance their risk management. Alongside this national policy, we are amending our tax law to cut profits tax of the business of offshore risks of captives by half, starting from the current tax assessment year of 2013-2014."

The Inland Revenue (Amendment) (No 3) Bill 2013 was introduced into the Legislative Council on 8 January.

"While widely adopted by multinational corporations in the US and Europe, captive insurance is relatively underutilised in Asia. That is why we had the idea of organising this workshop during the Asian Financial Forum. We hope to put the spotlight on insurance and stimulate more discussions on captive insurance in Hong Kong," King-chi added.

Attending the workshop as panellists were James Wong from Aon Global Risk Consulting in Asia Pacific, CEO of Peak Reinsurance Company Franz Josef Hahn, and assistant commissioner of insurance Ros Lam. Managing director of Jardine Lloyd Thompson, Nick Cousins, was the moderator at the workshop.

Wong said: "The reasons for corporates to form captives are saving from insurance expenses, strategic risk management and cash-flow management. Financial institutions, health-care services industry and manufacturing industry are heavy users of captive insurance."

Hahn said that reinsurance could absorb the excess risk exposure from captives through

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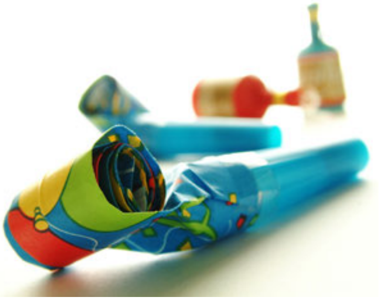


risk transfer. "Hong Kong's advantages as an insurance hub are robust legal and regulatory systems, and easy access to other markets in the region."

Lam emphasised that the process for applying for authorisation of a captive insurer could be completed within three months, and the annual fee for captive insurers is only $22,600.

In his concluding remarks, deputy chairman of the Hong Kong Federation of Insurers, Jimmy Poon, said: "The Hong Kong Federation of Insurers has set up a task force to steer the promotion of Hong Kong as a captive insurance hub. With all the infrastructure and expertise we have in our market, together with the proactive support of the Hong Kong government with tax concessions as the first step, we are well equipped to bring this forward."

Montana reaches the 150 captive mark

Montana gained 36 new captive insurance companies and risk retention groups in 2013, bringing the total number of licences to 150 at 31 December 2013.

The Office of the Montana Insurance Commissioner reported that the Treasure State experienced a net gain of 36 new captive insurance companies and RRGs to the state in 2013, bringing the total number of licences to 150 at 31 December 2013 compared to 114 a year ago.

Aceterrus, an independent captive management firm based in the northwest of the US, said that of particular interest in the results was the formation of two new series limited liability companies licensed as captive insurers, one of which was organised by Aceterrus Insurance Resources.

Including the series LLCs in the number of Montana captive licences, Montana had 160 active licenses for captives and RRGs at the end of 2013.

Series LLC captives are a new structure in Montana, with the state's captive insurance association drafting series LLC legislation that was enacted and became effective on 1 October 2013.

Brenda Olson, chair of Montana's captive association and managing director of Aceterrus, said that in 2010 the Internal Revenue Service provided clarification on the tax elections possible for series LLCs that helps reduce tax risk for these businesses.

"Series LLCs are cost effective for nearly any industry, including captive insurance and real estate organisations."

A report from Aceterrus said that Montana continues to thrive as a successful captive domicile, plowing through the 100-captive wall that blocks other US captive domiciles such as Arizona, Nevada, and South Carolina.

It attributed Montana's success to: a business friendly regulatory and legislative environment; flexible laws allowing a wide variety of licensing options; continued investment in regulatory support resources from the insurance commissioner; and an extremely low tax environment, whereby insurers are not subject to Montana state income taxes and further enjoy nominal licensing and preferential premium tax rates.

Tax court finds Bermuda to be genuine captive

The US Tax Court has ruled that payments to Rent-a-Center's wholly owned captive, located in Bermuda, were deductible as an insurance expense.

The Tax Court majority found that the Bermuda-based captive was a genuine insurance company because it was created for significant, non-tax reasons and that there was no impermissible circular flow of funds.

The opinion of the Tax Court majority next turned to address whether the policies at issue involved insurance risk, concluding that the premium payments made by the taxpayer's subsidiaries to the captive subsidiary were deductible.

The opinion relied on a similar case that was heard in 1989, involving Humana Inc, for a significant portion of its analysis.

The case is among a number of similar lawsuits that aim to define what constitutes an insurance company.

Julia Rathgeber to speak at Texas conference

The Texas Captive Insurance Association has announced the agenda for its first annual conference in February.

Speakers will include insurance commissioner Julia Rathgeber and Republican John Smithee, chairman of the Texas House of Representatives insurance committee.

The Texas Department of Insurance began accepting applications from prospective captives in November 2013.

The Texas statute requires that parent companies have significant operations in Texas in order to form a captive in the state. The bill passed in Texas prohibits captives from accepting insurance policy risks of an insurance affiliate.

The association was formed in June of the same year.

Gibraltar aims to be gateway for AIFMD

Gibraltar has become a full signatory to the Multinational Memorandum of Understanding of the International Organization of Securities Commissions (IOSCO)—a regulatory move that positions the territory as a gateway to the Alternative Investment Fund Managers Directive (AIFMD) zone.

Nicola Smith, managing director of hedge fund administrator Helvetic, said that the signing bolsters Gibraltar as a location for international hedge funds looking for a geographic foothold within the AIFMD zone.

The passport system established under AIFMD allows funds to operate throughout the EU once they have received regulatory approval in a single member country.

The result has been an increased level of interest from international fund managers seeking territories that blend a skilled workforce, high quality provision of services such as audit and administration, and a regulatory framework that meets international standards.

The memorandum is one more significant step that positions Gibraltar in the global market as a gateway to the EU.

Smith said: "We will see 2014 as the first year which requires hedge fund managers to take positive action in response to the AIFMD. Key to the changes introduced by the legislation is the better transparency through increased monitoring and reporting on risk management and investment activities."

Guy Carpenter expands on capacity report

A new report from Guy Carpenter highlighted the significant fall in rates on line. It Attributed this fall to relatively low loss experiences, strong balance sheets and an influx of capital that spurred competition and innovation in the reinsurance market.

This means that the marketplace focused on meeting individual client needs to combat the challenge posed by alternative markets. Insurers also aimed to adapt their buying strategies and prioritise their risk transfer goals.

Asked about the continued increase in retention levels on the primary side, David Flandro, head of global business intelligence, said: "Premium retention rates have been increasing since 2009. However, it is somewhat of a paradox. Primary insurers are retaining more at a time when the cost of debt is increasing, the cost of equity is increasing and the cost of reinsurance is falling. Why is the sector retaining more?"

"It is our job as brokers to understand the corporate objectives of each of our clients and to gain a full understanding of their coverage needs. That is how we will encourage companies to reduce their retention levels and increase their reinsurance purchases."

Guy Carpenter's property catastrophe reinsurance rates on line index fell by 11 percent. The US in particular faced a 15 percent decline, while property catastrophe pricing in the UK and Europe also came under pressure, with rates falling by between 10 and 15 percent. This is the first renewal in over a decade where all major territories have seen pricing fall.

Conversely, the cat bond sector showed continued growth. Flandro said: "[Last year was] a record year in terms of cat bond issuances. In 2013, we have seen $7.1 billion in cat bond issuances. However, perhaps more importantly, total secondary capacity outstanding at the end of the year stood at $18.6 billion. The market is clearly growing and the appetite for this product is simply greater than what can currently be provided."

In his concluding comments, Nick Frankland, CEO of Guy Carpenter's EMEA operations, called for closer co-operation between the insurance and reinsurance sectors in order to enhance product development and better meet client needs.

"The challenge for the reinsurance industry is firstly to look at what it is delivering as a basic product to the insurance sector. Then it is for us to go to the insurance industry and assess the products that they are delivering to the commercial world and the public at large."

"It is clear that the insurance industry is simply not taking on enough risk. We have to find a way of bridging this gap. If the insurance sector cannot meet the needs of all of their clients, then we will have to work with them to encourage them to deliver the required solutions by bringing in the reinsurance capacity to support their efforts."

Bermuda Stock Exchange buoyant in 2013

The Bermuda Stock Exchange (BSX) has published its year-end review, confirming that 2013 was a strong year for the exchange, with a significant increase in the listing of insurance linked securities (ILS).

BSX president and CEO Greg Wojciechowski said: "[Last year] ended strongly with a record number of ILS listings, well-supported and successful Bermuda government bond listings and the smooth implementation of upgraded exchange mission critical technology."

"The accomplishments of the BSX to date and in particular this year resulted from the hard work of a dedicated team of stock exchange professionals that manage and operate the exchange on a daily basis."

At the end of 2013, there were a total of 665 securities listed on the BSX. Included in the new listings were several additional variable rate notes and programmes from Armor Re, Galileo Re, Loma Re, MetroCat Re, Nakame Re, Sanders Re, Tradewynd Re and VenTerra Re.

ILS numbers listed on the BSX grew 103 percent from 38 to 77. The value of these securities grew to $9.71 billion from $5.81 billion from the same period in 2012.

BSX chief compliance officer James McKirdy said: "Year-on-year listings grew by 32 securities in challenging global economic conditions. In particular, new listings grew by 81 securities including 42 insurance linked securities with a capitalisation value of $4.617 billion."

Wojciechowski said: "I am delighted with the place we find ourselves as we begin 2014 and have every confidence that the hard work undertaken at the BSX and in Bermuda to create and sustain a reputable and respected commercial and regulatory environment will continue to drive commercial development and assist us in adding new lines of business and further elevate Bermuda's position amongst the major global financial centres."

New year sees muted demand from buyers

A number of converging factors has created a buyers market in nearly all lines of business, according to a report from Willis Re.

These factors include rate reductions, new capacity and market entrants, low interest rates, greater retention of reinsurance premiums by large buyers, diminishing reserve releases, expansion in terms and conditions, and increasing regulatory oversight.

John Cavanagh, CEO of Willis Re, said: “The key influence on the 1 January renewals has been overcapacity triggered by a number of converging factors. Strong 2013 results have bolstered traditional reinsurers’ already strong balance sheets. New capital from non-traditional capital market sources has grown to reach $50 billion.”

“These factors have been compounded by muted demand from buyers arising from the longer term trend of better regulation, which has in turn led to a better understanding and management of tail risk, as well as the trend of major insurance groups to retain more reinsurance premium volume and risk on their own growing balance sheets.”

The report also noted that soft market conditions are no longer unique to catastrophe business, with rates down on most lines. Pricing margins on excess of loss business have been compressed, and ceding commissions have increased on pro rata treaties for sought after clients with large ceded premium volumes.

Peter Hearn, chairman of Willis Re, said: “Faced with these market headwinds, reinsurers are adopting a variety of strategies. Larger reinsurers are using their balance sheet strength and technical ability to offer more capacity and more complex, multi-class, multi-year deals. Others are expanding into specialty lines and many have developed multi-channel capacity offerings seeking to use their underwriting expertise to deploy capacity on behalf of capital markets.”

Hawaii cell to slash healthcare costs

BevCap Management has formed a cell captive in Hawaii, to provide health benefits solutions for employers.

BevCap Sponsored Captive Insurance is a cell captive, with its first cell being BevCap Health, a heterogeneous group captive.

BevCap Health is a member-driven strategy to provide a health benefits solution for employers based on the desire to gain better control and reduce the costs associated with employee healthcare benefits. “[It] is an opportunity for employers to aggregate, share best practices, mitigate risk and bend the trend to reduce the long-term cost of healthcare benefits,” said a release from the firm.

BevCap Health is a self-funded health plan with group risk sharing. Members implement separate and distinct health plan designs, yet administer the plans as a group—leveraging the buying power of economies of scale. BevCap’s strategy is designed to correct the deficiencies driving dramatic year-over-year cost increases in the fully-insured market and help optimise current self-funded plans, added the statement.

BevCap Health was founded in February 2013 with a standard sales company out of Odessa, Texas. BevCap Health is comprised of five additional participants: Krey Distributing in St. Peters, Missouri, L&F Distributors in McAllen, Texas, Jordano’s in Santa Barbara, California, Andrews Distributing in Dallas, Texas, and TriEagle Sales in Tallahassee, Florida.

Together, BevCap Health covers 3000 employees.

John Coy of Andrews Distributing said: “The BevCap Group Health programme provides Andrews with a toolbox of individual benefits that will not only allow us to actively manage claims costs but also provide the highest degree of wellness for our employees.”

Easing the squeeze

The NAIC explains how lots of jurisdictions will benefit from reduced collateral requirements—and reveals Ireland, France and Japan's interest in the new model

GEORGINA LAVERS REPORTS

How did the process of reduced collateral requirements begin?

On 6 November 2011, the National Association of Insurance Commissioners (NAIC) adopted revisions to the Credit for Reinsurance Model Law (#785) and Credit for Reinsurance Model Regulation (#786).

These revisions serve to reduce reinsurance collateral requirements for non-US licensed reinsurers that are licensed and domiciled in qualified jurisdictions. Under the previous version of the Credit for Reinsurance Models, in order for US ceding insurers to receive reinsurance credit, the reinsurance was required to be ceded to US-licensed reinsurers or secured by collateral representing 100 percent of US liabilities for which the credit is recorded.

The revised models establish a certification process for non-US reinsurers—a certified reinsurer is eligible for collateral reduction with respect to contracts entered into or renewed subsequent to certification. Each state will have the authority to certify reinsurers, or a commissioner has the authority to recognise the certification issued by another NAIC-accredited state.

What are some examples of the evaluation criteria used?

Reinsurers are subject to certain criteria in order to be eligible for certification, as well as ongoing requirements in order to maintain certification. Examples of evaluation criteria include, but are not limited to, financial strength, timely claims payment history, and the requirement that a reinsurer be domiciled and licensed in a "qualified jurisdiction".

A state will evaluate a reinsurer that applies for certification, and will assign a rating based on the evaluation. A certified reinsurer will be required to post collateral in an amount that corresponds with its assigned rating (generally, Standard & Poor's ratings of "AAA" = 0 percent, "AA" = 10 percent, "A" = 20 percent, "A-" = 50 percent, "BBB+" = 75 percent, and "BBB" or below = 100 percent), in order for a US ceding insurer to be allowed full credit for the reinsurance ceded.

How did the NAIC come to the conclusion that Bermuda, Switzerland, Germany and the UK are suitable for reduced reinsurance collateral requirements?

At the 2013 Fall National Meeting in Washington DC, the NAIC approved four international supervisory authorities as Conditional Qualified Jurisdictions under the Process for Developing and Maintaining the NAIC List of Qualified Jurisdictions.

The four jurisdictions are the Bermuda Monetary Authority (BMA); the German Federal Financial Supervisory Authority (BaFin); the Swiss Financial Market Supervisory Authority (FINMA); and the UK's Prudential Regulation Authority of the Bank of England (PRA).

These four jurisdictions were placed on the NAIC List of Qualified Jurisdictions effective 1 January. The NAIC will proceed with its full review of these four jurisdictions during 2014, upon which they will be approved for a five-year period.

Are there any other jurisdictions already on the NAIC List of Qualified Jurisdictions—and can you say which jurisdictions are in consideration?

Currently, 18 US states have adopted the revisions to the credit for reinsurance models, with about five additional states considering similar proposals.

These states are Alabama, California, Connecticut, Delaware, Florida, Georgia, Indiana, Iowa, Louisiana, Maine, Maryland, Missouri, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island and Virginia. Insurers domiciled in these 18 states write approximately 53 percent of the primary insurance premium in the US (the additional five states would raise this market share to approximately 75 percent).

Each state may evaluate the reinsurance supervisory system of a non-US jurisdiction in order to determine if it is a "qualified jurisdiction." The NAIC has also drafted a process for developing and maintaining a list of qualified jurisdictions.

A state must consider the NAIC list in its determination of qualified jurisdictions. The list is not binding, but a state must thoroughly document the justifications for approving any jurisdiction not on the list.

The NAIC will begin discussions with other supervisory systems interested in being considered for inclusion on the NAIC List of Qualified Jurisdictions. To date, the NAIC has received enquiries with respect to Ireland, France and Japan.

How do you think that the US is modernising reinsurance? What else needs to be done?

The amendments to the NAIC Credit for Reinsurance Models are part of a larger effort to modernise reinsurance regulation in the US.

In 2007, in light of the evolving international marketplace, the NAIC determined that the timing was appropriate to consider whether a different type of regulatory framework for reinsurance in the US was warranted.

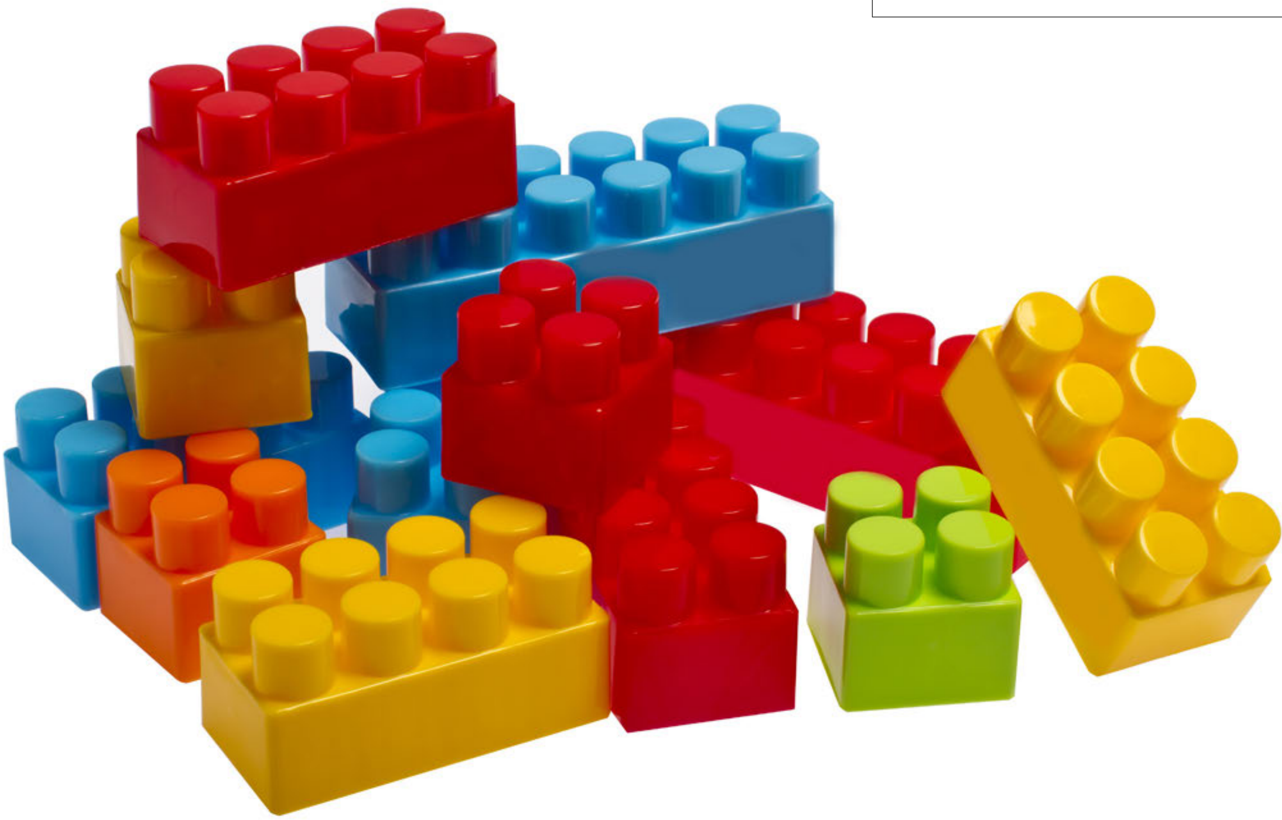
The Reinsurance Regulatory Modernisation Framework proposal was a conceptual framework that was developed by the reinsurance (E) task force during 2007 and 2008 in response to its charges to consider the current collateralisation requirements regarding unauthorised reinsurers, and to consider the design of a revised US reinsurance regulatory framework.

The reinsurance framework was intended to facilitate cross-border reinsurance transactions and enhance competition within the US market, while ensuring that US insurers and policyholders are adequately protected against the risk of insolvency.

The NAIC adopted the framework during its 2008 Winter National Meeting. The 2011 revisions to the Credit for Reinsurance Models were based on the 2008 framework and are intended to implement reinsurance collateral reduction within the state-based insurance regulatory system.

What is the association's plan for the future?

The NAIC has committed to do the following: undertake a re-examination of the collateral amounts within two years from the effective date of the revisions to the models (eg, 6 November 2013); and revisit the issue of state uniformity in the adoption of the models within three years of the adoption of the new accreditation standard by the NAIC (eg, 9 April 2016). CIT



How and why you should set up a captive

David Herratt of the Labuan International Business and Financial Centre explains what goes in to the decision to establish a captive

Seventy-five percent of the world's Fortune 500 companies are parent owners of captive insurance companies. More than 5000 captives have been established worldwide, with a total of captive premium income exceeding $14 billion. There are different types of captives, such as single-parent captives, rent-a-captives, protected cell companies and special purpose vehicles.

How does a captive work?

A captive is essentially a wholly-owned insurance company, usually located in a jurisdiction where taxation, solvency and reporting requirements are relaxed. They are usually managed by specialist companies that act as accountants and administrators. However, much of the decision-making pertaining to the risks being retained by the subsidiary company or transferred to the conventional insurance market, are undertaken by the parent company (parent).

A captive must operate as a true insurance company. The need for annual actuarial reviews, yearly financial statement audits, continuing tax compliance oversight, claims management and other regulatory compliance needs puts the day-to-day management of a captive beyond the skills of most general business people. The use of an experienced and capable captive management company is an essential element in a captive's operations.

The cost of 'self-insurance' outside of a valid and qualifying captive structure is not tax-deductible. A properly formed and operated captive may, however, deduct insurance premiums that are paid into a privately-owned insurance company. Claims are paid with pre-tax dollars. If no claims are made, the captive retains the premiums for future business risks or distribution.

Formation of a captive

The formation of a captive involves the following processes: feasibility studies, financial projections, determination of domicile and lastly, preparation and submission of application for an insurance licence. The need for a qualified insurance manager on the planning team is therefore very important, particularly in the formative stages.

The requirement for adequate initial capitalisation of the captive is dependent in part on the level of risk projected to be assumed by the captive (risk appetite) and the domicile chosen.

Legislative and regulatory issues to be considered when establishing a captive include identifying a sensible legal framework, choosing the appropriate type of entity, and evaluating its track record and cost and taxation advantages.

The decision to form a captive should be predicated upon the incorporation of formal and robust risk management procedures and culture within an organisation. Increased awareness and implementation of risk management practices is perhaps the most important reason for forming a captive.

There are numerous advantages to forming a captive, with the main drivers being risk management and risk financing:

Lower insurance costs

In establishing a captive, the parent seeks to retain profits within the group rather than have it go to an external party. A captive may also help reduce insurance costs by charging a premium that more accurately reflects the parent's loss of experience. Commercial market insurance premiums must adequately meet the cost of claims. However, in common with other commercial enterprises, insurers are in business to make money and will therefore include in the premium an element to provide for their acquisition costs, overheads and profit. This portion of the premium can represent as much as 35 or 40 percent of the whole transaction.

Cash flow benefits

By utilising a captive, premiums and investment income are retained within the group and, where the captive is domiciled offshore, that investment income may be untaxed.

Additionally, the captive may be able to present a more flexible premium payment plan, thereby offering a direct cash flow advantage to the parent.

Apart from pure underwriting profit, insurers rely heavily on investment income. Premiums are typically paid in advance while claims are paid out over a longer period. Until claims become payable, the premium is available for investment.

A company's willingness to retain more of its own risks, particularly by increasing deductible levels, may be frustrated by the inadequate discount offered by insurers to take into account the increased deductible and by the fact that the company is unable to establish sufficient reserves to pay future claims. Establishing a captive can help address both of these problems.

Increased coverage

A captive may provide the coverage required where the commercial market is unable or unwilling to provide coverage for certain risks or where the price quoted is seen to be unreasonable.

Link to risk management

Risk management can be viewed by a captive owner not as a cost centre but as a potentially profitable part of the company's activities. A captive acts as a focus for the risk management and risk financing activities of its parent organisation. An effective risk management programme will result in recognisable profits for the captive.

A captive can also be used by a multinational to set global deductible levels, enabling local managers to insure with the captive at a level more suitable to the size of their own business unit while the captive only buys reinsurance in excess of the level appropriate to the group as a whole.

Access to the reinsurance market

By using a captive to access the reinsurance market, buyers can more easily determine their own retention levels and structure their programmes with greater flexibility. Reinsurers are the international wholesalers of the insurance world. Operating at a lower cost structure than direct insurers enables them to provide coverage at advantageous rates.

Underwriting unrelated risks for profit

Apart from writing its parent's risks, a captive may operate as a separate profit centre by underwriting the risks of third parties. In particular, an organisation may wish to sell insurance to existing customers of its core business. For example, a retailer may sell extended warranty coverage to customers with the risk being carried by the retailer's captive. The claims pattern of this type of business is usually very predictable, with a large number of small exposures, and can provide the retailer with a valuable additional source of revenue.

Tax minimisation and deferral

The tax considerations in forming a captive will depend on the domicile of both the parent and the captive. Integration of a captive as part of an overall tax planning strategy is a complex subject and professional legal and tax advice is essential.

Insurance benefits

The establishment of a captive provides a greater degree of flexibility and control over the risk management function. Insurance programmes can be designed in response to specific coverage, premium and retention requirements, and offer individual operating units of a company the coverage and deductibles they require, with the programme's overall control and design maintained at the corporate level.

Thus, captives can help centralise the financial and administrative operations of a corporate insurance programme. Captives can also be used as vehicles for funding risk exposures should a company decide to self-insure, or if commercial insurance coverage is unavailable or uneconomical.

Captive owners have found that owning a captive brings much more focus to the derivation and amount of losses being incurred. This leads to a greater emphasis on loss prevention programmes and the captive's use in measuring the impact of such programmes.

Is your organisation ready to form its own captive?

The use of a captive should be considered for entities that meet the following criteria:

- Profitable business entities seeking substantial annual adjustable tax deductions;
- Businesses with multiple entities or those that can create multiple operating subsidiaries or affiliates;
- Businesses with $500,000 or more in sustainable operating profits;
- Businesses with requisite risk currently uninsured or underinsured;
- Business owners interested in personal wealth accumulation and/or family wealth transfer strategies;
- Business owners seeking asset protection. CIT

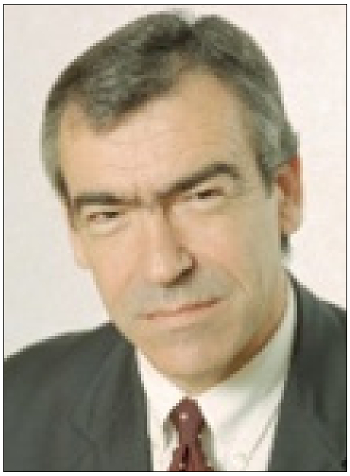
Benefits of establishing a captive in Labuan

As Asia Pacific's preferred international business and financial centre, Labuan presents investors with an ideal balance of fiscal neutrality and certainty.

The benefits of establishing a captive in Labuan include:

- **Robust and internationally recognised regulatory framework**: clear legal provisions and industry guidelines are provided and enforced by Labuan IBFC's regulator, the Labuan Financial Services Authority (FSA).
- **Facilitative and business-friendly legislation:** businesses in Labuan are governed by eight modern acts, including the Labuan Islamic Financial Services and Securities Act 2010, which is the world's first omnibus legislation governing all shariah-compliant financial services in an international business and financial centre.
- **Wide choice of entities:** Labuan has a broad range of entities and business and investment structures to cater to cross-border transactions, business dealings and wealth management needs.
- **Strategic location in the Asia Pacific region:** Labuan shares the same time zone with major cities in the region, such as Hong Kong, Shanghai and Singapore, which makes business dealings much more convenient.
- **Tax efficiency:** Labuan offers global investors and financial services providers a competitive tax structure and various tax exemptions, as well as access to the majority of Malaysia's extensive network of more than 70 double-taxation treaties.
- Penetration into Malaysia's insurance **market:** Labuan provides access to Malaysia's strong direct insurance market and offers preferential treatment due to domestic insurance tiering.

For more information on Labuan captives, please visit **www.libfc.com**.



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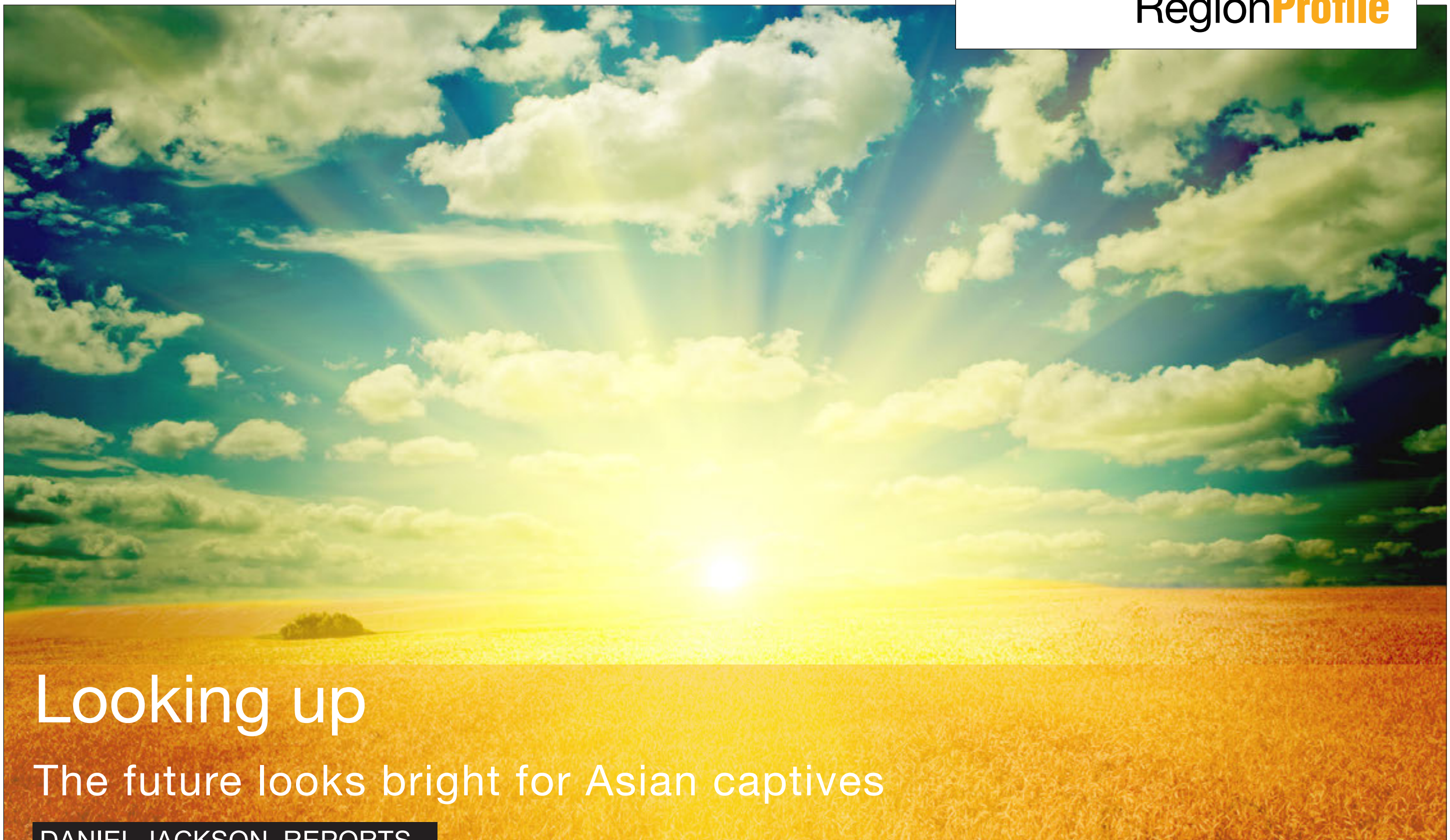

Looking up

The future looks bright for Asian captives

DANIEL JACKSON REPORTS

The captive market in Asia is still small compared to that of the rest of the developed world, but it is growing. Analysts predict that growth in this region will outstrip all other regions for at least the next decade, although it is admittedly starting at a low bar.

Jerry Xu, chief executive of Direct Captives, a captive service provider in Shanghai, is optimistic about the future of Asian captives.

"The growth we have seen is phenomenal. Yes, there are problems that we will encounter, as with all new ventures, but I have seen big changes in recent years, and I think there is now the momentum for self-insurance to be Asia's next success story."

The European economy has stalled over the last six years, while the Indian economy has grown by a third and the Chinese economy by 50 percent. It is this growth that has made Asia attractive to captives.

However, the Asian captive market is unusual in that it is not immediately clear who it is attractive to. Due to the development of the industry happening at such a glacial pace, the risks covered tend to be quite run-of-the-mill. As a place to domicile a captive, it can't be said to have found a niche, as even particular US states have.

The one area where it does excel is in taxation, which is significantly lower than other regions. This immediately raises concerns for some prospective clients. Is the regulation in this part of the market too relaxed? Xu doesn't think so.

"Understanding is on the increase. Captives were hardly known here just a few years ago, and so although it will take time, the regulatory regime will grow with the industry. There is perhaps a tendency for regulators to deal exclusively with local companies as a matter of routine, but this will change out of necessity in the years to come, as the market expands."

Lost in translation

Another factor to take into account when considering the insurance market in Asia is the cultural difference between the continents. In parts of Asia, insurance is not always a prerequisite for undertakings such as car or home ownership, as it is in Europe and the US.

The captive structure reduces insurance costs and controls losses effectively, but it requires a strong, stable insurance sector with a high level of market penetration. In the event of an accident resulting in an insurable loss, a lawsuit is much less unlikely to be the result than it would be in the US and Europe, where it is practically a foregone conclusion.

However, Xu belives that Asian captives can use this to their advantage. "It is true, we are not a particularly litigious culture. But I see opportunities for captives to expand into other areas, where our understanding of the mindset in this region is an advantage, for example, in takaful (Islamic) insurance."

Yet another factor is the level of state control over insurance, which varies widely between regions. For example, workers' compensation is covered by the government in Japan.

Previously, Asian companies wishing to form captives had few choices. The old offshore domiciles benefited hugely from this. Companies that have gone down this route are now in a position where their captives are so well established that a return to Asia would be difficult under the current regulatory environment in the region.

Xu believes that this is not an insurmountable problem, because "the bottom line matters".

"I think this will be true for the foreseeable future, but ultimately the bottom line matters, and if companies can get a better deal elsewhere they may just be tempted back. There are of course other advantages in having a local captive, including the opportunity to shape the future regulatory environment."

The competition

Despite its relatively high minimum solvency requirements, Singapore is the largest captive domicile in Asia, with more than 60 licensed entities, according to industry estimates. Captive registrations have slowed since other regions have opened their doors, but the domicile is not resting on its laurels. In recent years it has proposed a number of new guidelines to stay competitive. These are in relation to unrelated party risks, which will further tighten the regulatory system, which may prove attractive to larger, better established firms looking to start a captive.

Singapore is mostly host to Australian captives, but owing to the improving economic prospects in Asia, this can be expected to change in the future. CIT


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Solvency II: on the home stretch

The turn of the year marked the beginning of the two-year transitional period between individual national insurance legislation regimes and Solvency II

DANIEL JACKSON REPORTS

Politicians in the EU reached an agreement on Solvency II in November 2013, finally paving the way for the introduction of the legislation in January 2016.

The deal was agreed between the European Commission, the European Parliament and the Council of the EU after protracted negotiations.

The legislation was originally intended to harmonise the EU insurance industry, and to create a single market for insurance in Europe with a common floor of regulation. Since the financial crisis of 2008, it has also been touted as a way to protect taxpayers from exposure to the risks in the insurance sector. The commission aimed to establish EU-wide requirements for the industry on similar lines to those for banks, to negate the risk of a financial crisis emanating from the insurance sector.

The EU has come under criticism from several firms in relation to Solvency II. In August 2013, Tidjane Thiam, chief executive of Prudential, said that the proposed Solvency II regulatory framework represents "one of the biggest threats to UK jobs and growth". He said that the legislation could prevent the insurer and similar companies from investing in infrastructure and property.

Why is Solvency II required? Tim Edwards, a director at PricewaterhouseCoopers who was previously a part of the UK financial services authority's Solvency II team, believes that it is essential for the functioning of the single market.

"Solvency II started from a pretty simple place. Any consumer anywhere in Europe under freedom of services can buy insurance from any insurer anywhere in Europe. It therefore makes sense to have consistent standards for governance, risk and capital management, capital management, and some kind of public reporting regime so that there is at least a common floor of standards from a consumer protection perspective."

"Beyond that you can equally argue that the EU market is greatly helped by having commonality of regulations. If you are an insurer looking to set up elsewhere in Europe, you are under the same regulatory regime as you would be in the UK, in France, Denmark or anywhere else. Solvency II helps the single market in that respect by helping insurers to compete internationally. This is very different to captive domiciles, which effectively compete with each other from a regulatory perspective".

Big money

Insurers are Europe's largest institutional investors, with $11.3 trillion in assets under management. Unlike banks, insurers have no framework in place to mitigate against a repeat of the financial crisis, and this is one of the arguments that propelled Solvency II forward. With the implementation date fast approaching, transitional measures have been instated as of 1 January.

But are reinsurers ready to produce the Solvency II-compliant financial reports that they are now required to? Edwards thinks not.

"Nobody is ready yet as far as I am aware. There is a lot of work that needs to go in to be able to prepare for the reports. Most firms will need as much time as they have left in order to achieve it. However, there is no reason to think that reinsurers are going to have to do more than anyone else."

Many journeys

One of the problems for any piece of legislation going through the motions in the EU is the amount of individual nations that have to be satisfied before progress can be made. As each and every member state has the power to veto new legislation under the current treaties, lawmaking is notoriously slow. The solution that the EU has found to this is exceptions.

In December 2013, France rejected interim measures on governance during the two-year preparatory phase, with a promise to increase the pressure on firms to be compliant by 2016. Edwards does not see this as a major problem. "My understanding is that this is basically a procedural thing. You need to bear in mind that the preparatory guidelines are just preparing us for Solvency II in a couple of years. Every single country has certain limitations around what they can and can't do during that period. My understanding is that France informed the other member states that it can't actually enforce the preparatory guidelines, but nonetheless it has given a very clear instruction to their industry that they are expected to respect them and prepare in the way that the spirit of the regulations require."

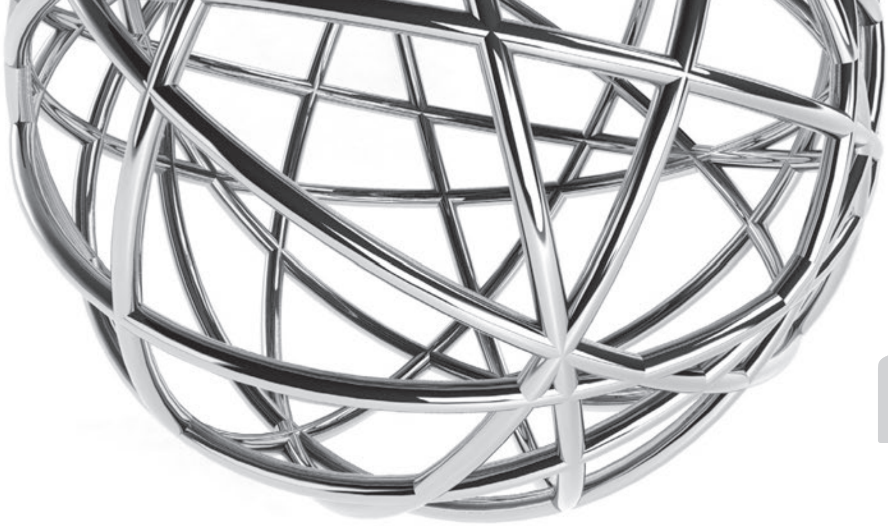
"Whilst we are trying to bring in a common system of regulation there are, of course, as many different legal and political systems as there are member states, and so there are bound to be a few wobbles between them. There is no indication that the French are not committed to Solvency II, in fact quite the opposite. Whilst it is the same destination, there are a lot of different journeys."

Market indifference

Given that a political agreement has now been reached on the legislation, many commentators expected this to be reflected in the results of equity markets.

Thus far, the reaction has been fairly muted. Edwards explains the lack of reaction by saying that analysts have done their job extremely well.

"Whilst it was quite a big moment when we realised that Solvency II was actually going to happen, I think analysts understood that the political direction was positive for quite some time. Throughout the second half of last year there was an expectation that the agreement was going to be reached, and so it wasn't really a one-off blinding light moment. Analysts will have taken account into the expectation of Solvency II over a period of time at which point it gets lost in a number of other things going on around the industry, whether that is issues in the international markets or local issues with individual firms." CIT



Gibraltar: a gateway to Europe

For standalone captives or cell captives, the British Overseas Territory provides the best of both worlds, says Robus Gibraltar's Tom Stephenson

For multinational companies with insurable risk throughout Europe, a domicile such as Gibraltar is often a natural choice for a captive. Gibraltar is a full member of the EU and as such, Gibraltar insurers benefit from access to the European market under freedom of services legislation. In practice, this means that any Gibraltar insurer—whether captive or open-market—can write insurance for policyholders in any European economic area (EEA) state. As a result of this, Gibraltar's insurance industry has grown significantly over the past 20 years and is increasingly seen as the gateway to Europe.

Needless to say, Gibraltar must compete with other major domiciles for a share of the captive market, however, the competitive landscape is varied and uneven. Malta, Dublin and Luxembourg all provide some degree of competition and each domicile tends to appeal to particular types of business. Gibraltar is unique in that it scores highly in every category. It has an accessible regulator, a benign tax regime, a legal system based on English law and a developed infrastructure. Gibraltar also offers a number of additional practical benefits too—for example, a predominantly bilingual workforce (English and Spanish), which has particular appeal to North and South American organisations.

Establishing a captive in Gibraltar

Establishing a captive insurer in Gibraltar is a relatively pain-free process, certainly compared to the larger European jurisdictions. Most parent companies will appoint a captive manager on the ground in Gibraltar. The captive manager will typically project manage the application process in order to get the captive licensed and established. The application process usually takes around four months, which compares well to other reputable onshore EU domiciles. Once the captive is licensed in Gibraltar, the insurance manager will submit a request to passport under freedom of services to the Gibraltar regulator, which in turn, informs their counterpart in the destination EU state. It's very straightforward and in our experience, the system works very well.

When passporting into other European states, it is doubly important for the captive board to remember its obligations for retaining 'mind and management' in Gibraltar, particularly if the captive is righting third party (eg, customer) business via another subsidiary. This means, among other things, that the captive must ensure strategic control remains in Gibraltar and that the captive is not used simply as a pot of capital. The captive manager will usually provide advice and assistance in ensuring that the company satisfies these obligations.

> A particularly capital-efficient way to access EU passporting is with a fronting insurer. Typically, this involves establishing a non-EU reinsurance captive and using a fronting insurer in an EU jurisdiction through which to access other EU states

In addition, insurance premium tax rates differ throughout Europe and the captive or its manager must ensure these are remitted to the relevant authorities. There are a number of European countries with notoriously convoluted insurance premium tax regimes and advice should be sought where appropriate.

Non-EU reinsurers and fronting

Of course, with EU membership comes EU minimum solvency requirements. Undeniably, this can put off a number of potential captive owners for whom capital is tight, but for many multinational captive owners it is a price worth paying for the flexibility and access that EU passporting rights provide.

There are other options, however, and a particularly capital-efficient way to access EU passporting is with a fronting insurer. Typically, this involves establishing a non-EU reinsurance captive and using a fronting insurer in an EU jurisdiction through which to access other EU states. In a recent example, a UK parent company established and capitalised a Barbados reinsurance company to underwrite the risks emanating from its subsidiaries in the UK, France and Germany. The reinsurance captive provides 100-percent quota share reinsurance to a Gibraltar fronting insurer, which ultimately issues the policies. In return, the Gibraltar fronting insurer receives a 'fronting fee' to compensate it for capital usage, credit risk and administration. There are a number of benefits to this approach, in particular, its capital efficiency.

By utilising the fronting model, the parent company has the freedom to establish a captive, albeit a reinsurance captive, in a wider variety of domiciles such as Guernsey or Barbados. In these jurisdictions, capital requirements are generally lower and set-up times considerably shorter. By way of comparison, the minimum solvency requirement in Guernsey is £100,000, whereas in European states the regulator will usually expect in excess of £3-4 million. The fronting vehicle can be either a standalone company or a 'cell' within a protected cell company (PCC) or incorporated cell company (PCC). A PCC is one legal entity divided into the 'core' and multiple 'cells'. The assets and liabilities of each cell are legally segregated from those of the core and all other cells (a cell within an ICC works in a very similar way, however, each cell has a distinct corporate entity). In other words, for the purposes of facilitating a reinsurance transaction, a cell can perform a very similar function to a standalone company.

Indeed, cells can be even more cost effective and capital efficient than a standalone reinsurer. For example, the core of the PCC will already have an insurance licence and will already meet the regulatory capital requirement. It will also have in place arrangements for the overall management of the entity, leaving the cell to get on with transacting reinsurance.

Often, the challenge for many captive reinsurers, whether cell or otherwise, is finding a suitable fronting partner. A great deal depends on the requirements of the parent; whether it requires a rated insurer, for example.

For most pure captive arrangements, however, a rating is not required though the financial robustness of the fronting partner remains important.

The insurer must also be willing to accept the captive as a reinsurance counterparty—and at the right price.

It is important, therefore, to highlight the financial strength of the captive, its own reinsurance programme and its parent. Often, the fronting insurer will insist on a number of contractually clauses in the policy documents and reinsurance agreements to mitigate its credit risk, though this depends largely on the perceived risk profile of the captive. A more burdensome risk mitigation measure is the requirement for a letter of credit (LOC), which can be expensive and often inefficient.

Fronting fees can vary from around 2.5 percent for large or low-risk programmes to around 10 percent for smaller or high-risk programmes.

Gibraltar is an excellent place to find a suitable fronting insurer. Gibraltar, as mentioned above, is an EU domicile and all insurers have European passporting rights. There are a number of insurers in the market with the appetite and capability to front European captive programmes. Set-up times can be very quick, particularly if the fronting insurer is already licensed in the relevant classes and passported into the relevant territories. If not, the process can take a little longer.

The implications of Solvency II

The fronting model is due to be tested as regulators in Gibraltar and elsewhere begin rolling out the final elements of Solvency II ahead of the official implementation date in 2016. Though the fundamentals of the model will not necessarily change, the costs for reinsurance captives will inevitably increase. Non-EU reinsurance captives will be faced with increasing demands for LOCs and parent company guarantees, as well as cut-through clauses, ensuring the fronting insurer has recourse to the captive's own reinsurers. Of course, in a Solvency II world, there are a number of ways for the non-EU captive to appear more attractive to potential EU fronting partners, by for example, obtaining a rating. Ultimately, despite the absolute increase in costs, any changes in the relative costs of the reinsurer-fronting model versus the standalone EU captive will be less significant.

Gibraltar is right to claim the title of 'gateway to Europe'. For standalone captives or cell captives, it provides the best of both worlds. It has an accessible and knowledgeable regulator, EU membership, cultural and legal familiarity, a bilingual workforce, and a developed infrastructure. Equally, for non-EU captives, Gibraltar offers an excellent market in which to find high quality fronting insurers with capacity and appetite for new business. In any case, the captive reinsurer and fronting insurer model can be a particularly capital-efficient structure. **CIT**

Tom Stephenson
Director
Robus Gibraltar

Gibraltar PCCs and their future

What's on the cards for protected cell companies in Gibraltar? Alain Dufraisse of Aon Insurance Managers and White Rock Insurance takes a look

Since the enactment of the first legislation at the end of the last century, a lot has happened on the protected cell companies (PCCs) front.

Firstly, there are an ever increasing number of jurisdictions that have implemented similar regulations. Although the name of such companies might differ (eg, segregated portfolio companies or segregated account companies) depending on the jurisdiction, the basic legal principle remains the same: a cell company is a corporate vehicle that is permitted to segregate its assets and liabilities between different cells of itself, for different purposes, with the result that a creditor's recourse against the cell company is limited to whichever cell was transacted with. Where a cell becomes insolvent, the remaining cells of the structure are not affected and continue to operate as normal.

The cell company regulations therefore addressed the perceived weakness of rent-a-captives where assets being pooled, users are insecure about their exposure to unlimited liability in the event of a claim by one or more of the other users. Whereas traditional insurance, through the common fund mechanism, ie, pooling, demands that the premiums of the many fund the losses of the few, PCCs ensure that their premiums are protected against the losses of the many.

There are now more than 50 jurisdictions around the globe that have adopted cell company regulations, and this number is expected to grow further, while established domiciles such as Gibraltar continue to adapt their regulations to an ever changing environment. This clearly demonstrates that the PCC concept has gained international recognition and that it is becoming an increasing alternative in insurance placements for the years to come.

Gibraltar

Gibraltar has always been at the forefront of PCC promotion and use, being the first EU jurisdiction to promulgate a PCC Act, in 2001. Before this, only offshore domiciles had similar legislative frameworks and Gibraltar saw the opportunity offered by its EU jurisdiction status to enhance the concept further and combine cell solutions with the ability to write direct insurance across the EU/European economic area (EEA) on a freedom of services basis.

This proved to be a very wise move from the Gibraltar insurance industry stakeholders and legislator, as is for example demonstrated by the success of White Rock Insurance (Gibraltar) PCC Ltd the first ever EU-based PCC. Since its establishment in 2002, White Rock has established more than 50 cells and currently has 22 open cells, which makes it by far the largest PCC in the EU.

Other PCCs, whether life or non-life companies, have set up in Gibraltar to avail of its favourable legal framework and ability to 'passport' across Europe.

Various factors explain this success, but one key element remains the unparalleled speed (at least in the EU) at which the Gibraltar Financial Services Commission is able to license PCCs and authorise individual cells. This, combined with the pragmatic and proportionate approach taken by the Gibraltar regulators, gives the visibility and clear framework indispensable for the conduct and development of business.

The various uses of cell companies

Cell captives

Cell captives can be used to assist clients who wish to retain their own risk, as they would do with a standalone captive. This is no doubt the main use of cell companies for insurance purposes.

Typically, this solution may suit companies that do not wish to meet the minimum capitalisation requirements imposed in the EU because the programme they want to write is too small to efficiently leverage the minimum capital required. There can also be cost efficiencies for companies using a cell captive as opposed to a standalone captive. A PCC may also suit clients with specific needs or that require a shorter-term solution than the commitment of owning a captive, as they incur lower formation and operating costs and have much faster entry and exit strategies, than the captive alternative.

Fronting cells

The participants of the 2013 study conducted by the Captive Insurance Companies Association identified the traditional fronters' requirement for collateral as one of the three biggest challenges in owning a captive.

Thanks to the legal segregation of assets and to some contractual arrangements, the need for collateral is not as critical for PCCs. For example, the Aon-owned White Rock generally does not require collateral for pure fronting arrangements to captives or to the reinsurance market.

This partly explains the Gibraltar-based PCC's success in offering fronting cells to write its clients' risks across Europe (the company is licensed for all non-life classes of business), allowing them to access the reinsurance markets or their captive. In the latter case, fronting is required either because the captive only has a reinsurance license (eg, Luxembourg reinsurance captives) or because they are established outside of the EU/EEA (eg, in Bermuda or Guernsey) and are therefore not licensed to write insurance across Europe on a freedom of services basis.

The objective for White Rock in this arrangement is to provide access to licensed paper. However it is important to note that where the cells operate as a 'pure front', the insured has generally no formal ownership or control over the activities of the cell. The transaction from the insured's viewpoint is no different from the traditional market.

Other uses

Thanks to the flexibility offered by these vehicles, PCCs lend themselves not just traditional captive purposes, but much more. For example, cells have been used successfully to facilitate and accelerate the run-off of all or part of some (captive) insurance companies. Cells are also increasingly being used in insurance-linked securities (ILS) to facilitate securitisations and to transform capital market products such as derivatives and catastrophe bonds into insurance products. In the same way and overwhelmingly, it is insurance risk that is transformed into financial risk or risk that the capital markets can accept.

For their part, life insurance PCCs tend to be used by high-net worth individuals who desire control, transparency and security over the management of their assets.

The main advantages for users of cell companies

Although most are inherent to the particulars of the cell company structure in itself, many of the advantages that the cell users can benefit from also depend on the approach and policies of the cell company promoter. The advantages generally enjoyed by users are as follows:

Cell captives

- **Lower formation costs:** reduced capital (no minimum for cells), zero legal costs since the cell structure has already been incorporated, and generally lower application/registration costs.
- **Lower running costs:** generally reduced management fees, no non-executive directors, lower audit fees, no individual cell regulatory return, lower cost of maintenance of fiscal reps network, lower annual regulatory fees, zero tax exempt fees, and zero filing fees, etc.
- **Easier and quicker set up and exit:** cell formation can take place in a matter of days/weeks and it is not necessary to appoint a liquidator to close a cell.

Fronting cells

- **Competitive fronting fees:** fees are generally charged on a variety of bases dependant on premium volumes, number of territories, and services provided, etc.
- **Continuity of cover:** fronting is sometimes the core product of the cell company promoter. In this case, unlike traditional insurers, the fronting offer is not dependent on the market cycles or on participation in other layers or lines of the clients' programmes. Clients can therefore expect continuity in the availability of fronting services.
- **Flexibility on wordings and limits:** as the promoter generally requires that the reinsurance agreement contains a 'follow-the-fortune' clause, wordings can therefore be more flexible than the traditional carriers that tend to impose their own wordings, exclusions and limits.
- **Often, no collateral required:** as explained above, the cell structure can allow its promoter to get out of the requirement for a letter of credit, parental guarantee, premium deposit or any other form of guarantee, generally imposed by traditional carriers, especially when fronting for captives is involved.
- **Speed of payment of the reinsurance premiums:** speed of payment of the reinsurance premiums is a key issue, especially when the reinsurer is the client's captive. Since fronting arrangements are made through dedicated cells, the promoter can contractually commit to pass the premiums over to captives or reinsurers within strict deadlines.
- **Specific advantages:** each promoter might develop specific niche products.

Other types of cells

Given the many other uses that can be made of cells, it would be impossible to give an exhaustive list of the advantages enjoyed by the cell users. However, in the main, cells provide an opportunity for a flexible structure, easy and quick set-up, and a cost effective solution to put in place and to maintain.

Solvency II: the next growth opportunity for Gibraltar PCCs?

The increasing number of new cell company jurisdictions will undoubtedly intensify competition and potentially dilute the revenue streams of the established domiciles. Practitioners and legislators in the competing domiciles will persist in attempting to differentiate their cell company products in the hope of creating a competitive advantage or just publicity.

There is no doubt that the Gibraltar insurance industry and the legislators will continue to work hand-in-hand to bring innovation and improvements to cell companies, instead of resting on their laurels.

Gibraltar, along with other EU jurisdictions, will have to implement Solvency II by 2016. However, although the directive might often appear a challenge, it will also bring opportunities, particularly for the existing and new Gibraltar PCCs that will benefit from the expertise, know-how and resources available locally, both within the industry and at the regulator.

Indeed, the directive may lead to increased costs that will particularly affect EU-based smaller captives and open market insurers. We have seen above the existing benefit of pooling the running costs of a PCC between its promoter and cell clients. The fact that a PCC is a single legal body that will have to comply as a whole is likely to make pooling even more pertinent when it comes to addressing the new requirements under all three pillars in terms of regulatory capital (Pillar I), governance (Pillar II—risk management, internal audit, investment and other committees, production of an Own Risk and Solvency Assessment, etc), and reporting/disclosure (Pillar III) requirements.

Inevitably, there will be situations where the resulting increases in costs associated with regulatory changes will result in a captive parent's decision to exit and shut down its standalone captive. In many cases, this is difficult to achieve and so a PCC provides the facility of 'rump warehousing' through which a particular block of risk is transferred to a cell in the PCC and the captive owner is effectively able to shut the captive subsidiary down, while being able to continue to self-insure through an EU-based cell. CIT

Alain Dufraisse
Director
Aon Insurance Managers (Gibraltar) and White Rock Insurance (Gibraltar) PCC

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Industry appointments

The Bermuda Monetary Authority has appointed **Andrew Gibbs** to the position of director of supervision for insurance.

Gibbs will report to Craig Swan, managing director of supervision.

Swan said: "We are delighted to attract staff with decades of business experience and technical expertise, such as Gibbs, in order to continue the effective implementation of a forward-looking risk-based supervisory framework that addresses the unique characteristics of Bermuda's financial sector."

Gibbs said: "I am pleased to be joining the authority at such a pivotal time for global regulatory change in the insurance and reinsurance industry. I am looking forward to working with my colleagues at the authority as we continue to build out the regulations here in Bermuda, as well as in ensuring that our practical risk-based approach to regulation continues to earn full credit in relation to global equivalency efforts."

For the past five years, Gibbs has held positions at Validus Holdings Ltd as executive vice president and head of internal audit following a period as the company's group controller.

Prior to that, he spent 12 years with the ACE group of companies as CFO of ACE Global Re as well as chief financial and operating officer of ACE Bermuda.

Jason Bundick is Healthcare Services Group's new general counsel and secretary. He will continue to serve as the company's chief compliance officer.

The company has also filed an application with the New Jersey Department of Banking and Insurance to form HCSG Insurance Corp, a captive insurance company.

The wholly owned captive insurance subsidiary will provide its parent company with certain insurance-related services. The company's vice president of human resources and risk management, **Andrew Kush**, will serve as president.

Additional executive officers of HCSG Insurance will include **Matthew McKee**, vice president and director of marketing, **John Shea**, treasurer and CFO, and **John Emslie**, secretary and associate corporate counsel.

In conjunction with the company's planned incorporation of HCSG Insurance, the company entered into amended and restated loan agreements with PNC Bank to increase its existing bank line and letter of credit availability to $125 million.

The proceeds available under the facility may be used for the funding of its captive insurance company as well as general corporate purposes.

Honigman Miller Schwartz and Cohn's board of directors have elected eight new partners in the firm, including **Scott Geromette**.

Geromette practices in Honigman's insurance department and is located in the firm's Detroit office. He focuses on the organisation and representation of a variety of alternative risk financing arrangements, including captive insurance companies, self-insurance programmes, risk purchasing groups, rent-a-captives and risk retention groups.

Geromette is particularly experienced in establishing captive insurance companies that become members of one or more of the Federal Home Loan Banks, said a statement from the firm.

In addition, he provides clients with reviews and interpretations of insurance policies and analyses questions of coverage. He also counsels owners/sponsors of alternative risk financing arrangements on legal, regulatory and strategic issues.

Barbican Insurance Group has appointed **Lucy Town** as an underwriter in the firm's non-marine reinsurance department.

Town will be underwriting US casualty reinsurance business and will report to Ondine Bourrut Lacouture, underwriting manager.

Town is an experienced treaty and facultative reinsurance underwriter who has worked across a range of lines including medical malpractice, professional liability and general liability.

Prior to joining Barbican, she was the lead underwriter for Aspen Re's US casualty book in London. She joined Aspen Insurance UK Ltd in September 2005 as an underwriting assistant, rising to the position of assistant underwriter in 2009.

Andy Caldwell, head of non-marine reinsurance, said: "During her eight-year insurance and reinsurance career, Town has achieved significant success, rising quickly through the ranks and amassing considerable experience across a range of territories and lines of business. She is a highly motivated individual with excellent analytical skills, and I and the team look forward to working with her in her new role."

Town said: "I am delighted to be joining the non-marine reinsurance team at Barbican. The company has built its market reputation upon the calibre of its underwriters, strength of its client relationships and its willingness to innovate and adapt in response to a changing market." CIT

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