CIT CAPTIVEINSURANCETIMES

ISSUE069
Conference Special

Roundstone Hits the Mark

Experience
Since 2003, Roundstone consistently delivers captive program solutions to a myriad of traditional and unique exposures.

Innovation
Roundstone invented the producer friendly incubator captive with turnkey underwriting facilities.

Focus
Committed to accurate quarterly reporting, fully executed agreements and transparent communication.

Results
Roundstone introduced stop loss group captives in 2005 and remains the largest manager of stop loss group captives today.

ROUNDSTONE
TURNING RISK INTO RESULTS

27887 Clemens Road, Westlake, Ohio 44145 , 440-617-0333
www.roundstoneinsurance.com ~ info@roundstoneinsurance.com

Atlas tells NAIC where to go

Atlas Insurance Management, a Charlotte-based captive insurance management firm, has written to the chairman of the National Association of Insurance Commissioners (NAIC) Financial Regulation Standards and Accreditation Committee to register its opposition to a draft proposal.

The proposal would subject certain captive insurers to "Part A" accreditation standards, which would require them to abide by the same laws applicable to commercial insurers.

The NAIC proposal would apply to any property and casualty or life and health captive operating in at least one state other than its state of domicile.

It would also apply to these captives reinsuring business that was directly written by a ceding insurer in at least two states.

"I firmly believe that captive insurance, just like commercial insurance, is a broad economic and social good, helping turn the wheels of commerce and allowing for-profit and not-for-profit entities to take and manage the risks inherent in the transaction of any business," said Martin Eveleigh, chairman of Atlas.

He added: "The adoption of this proposal would deny this good to many companies, including clients of Atlas, whose businesses operate across state lines."

Founded in 2002, Atlas operates offices in North Carolina and the Cayman Islands.

South Dakota to allow agency captives

South Dakota has amended Chapter 56-46 of its insurance code to allow the formation and regulation of agency captive insurance companies in the state.

House Bill 1180 defines an agency captive insurance company as: an insurance company that is owned, controlled or under common ownership or control by an insurance agency, brokerage, or reinsurance intermediary "that only insures the risks of insurance or annuity contracts placed by or through the agency, brokerage or reinsurance intermediary".

An agency captive can also be one owned or controlled by a producer of service contracts or warranties that only reinsures the contractual liability "arising out of service contracts or warranties sold through such a producer".

An agency captive in South Dakota may be formed as in the same manner as a pure captive—incorporated as a stock corporation, a non-stock corporation, a non-profit corporation, or formed as a limited liability company, business trust, or other form of legal entity as approved by the insurance director.

An agency captive formed in the state will be required to submit annually, no later than six months after the close of its financial year, a report of its financial condition using statutory accounting principles certified under oath by two of its officers.

Each captive will also have to provide a report of its financial condition audited by an independent certified public accountant every five years if it has annual direct premiums written of less than $2.5 million.

Anything exceeding $2.5 million will have to provide a report every three years.

New Bahamas captive scholarships

The Bahamas Financial Services Board (BFSB) and the Insurance Commission of the Bahamas have partnered to provide two full scholarships for the Associates in Captive Insurance (ACI) designation offered by the International Center for Captive Insurance Education (ICCIE).

ICCIE was developed in response to a need for in-depth educational offerings, information on current topics, and a professional designation. Despite a strong pattern of expansion in captive insurance companies, research has shown that there is a critical lack of education and training in the industry that, if not corrected, could affect its continued growth and professionalism.

The BFSB has said that the courses offered are relevant to any domicile around the world, and faculty members are recognised for their "expertise in captive insurance specialties".

The professional designation is the first and only comprehensive captive insurance education programme in North America.

The ACI designation includes five core courses, all of which can be taken via online, instructor-led asynchronous learning.

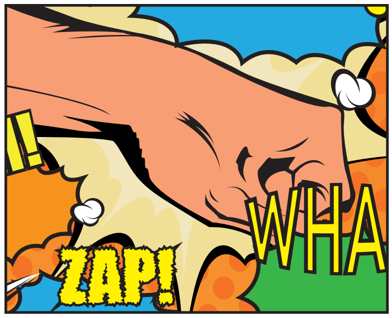
Roundstone offers new health plans

Roundstone Management and the Columbus Chamber of Commerce have entered into an exclusive captive partnership to offer self-funded health plans to employers with 20 to 500 employees in Ohio.

Gene Pompili, Roundstone's senior vice president of sales, commented: "We've been working closely to build a unique group captive solution for mid-market employers."

Jamie Zelewicz, vice president of Wells Fargo Insurance, said: "We have assembled the

CITINBRIEF



'A team' with Medical Mutual, Nationwide, Roundstone and Wells Fargo."

"This fresh approach offers chamber members a unique solution to leverage the purchasing power of the chamber, minimise expenses and risk, and position themselves to share in underwriting profits."

Roundstone said that the partnership reflects optimism about the continued growth of self-insurance and further expansion of the group captive's track record for delivering flexibility and transparency to better predict and control healthcare costs.

Guernsey hosts London ILS event

Guernsey Finance's most recent insurance-linked securities (ILS) event in London attracted more than 140 delegates and featured two panel sessions with ILS experts from Guernsey, the UK and mainland Europe sharing their expertise and insights into this fast developing asset class.

Dominic Wheatley, chief executive of Guernsey Finance, said the event was particularly timely as it coincided with the announcement by George Osborne, the UK chancellor, that the UK was committed to developing its own ILS regime.

"I believe the event demonstrated how Guernsey has established itself as a major destination for ILS business and that what sets it apart from other jurisdictions is its ability to innovate and to develop the technology that underpins the sector, rather than simply going after a large volume of transactions."

"Guernsey can boast a diverse range of transactions and risks across its ILS sector, including the reinsurance of satellites, lottery risk, football clubs and players, and marine reinsurance. The island's focus does not just revolve around traditional catastrophe risks," added Wheatley.

The fact that the UK has expressed an interest in ILS shows just how attractive the market is and we will watch those developments closely.

The event's first panel session focused on structural innovation, with a particular emphasis on the effects of cross-border regulations and structuring opportunities.

Moderated by Kate Storey of Appleby, the panel consisted of Christopher Bell of GBF Legal; Mark Helyar of Bedell Cristin; Nick Bugler of Wilkie Farr & Gallagher LLP; and Caroline Bradley from the Guernsey Financial Services Commission.

The second panel session looked at Guernsey as an ILS jurisdiction and its continued growth in collateralised reinsurance, longevity risk and the use of catastrophe bonds.

Moderated by Clive James of Kane, the panel consisted of Justin Wallen of Robus; Stewart McLaughlin of Willis; John Rowson of Aon; Martin Bird of Aon Hewitt; and Ben Canagaretna of Barbican.

Elizabeth Westwood, senior relationship manager at BNY Mellon, was one of those in attendance who appreciated the insight of the panellists.

"From a service provider's perspective, there was discussion about transactions that we have been involved in or had conversations about," she said.

"Particularly interesting in the second panel was the range of views. Everyone agreed there is a huge market but, on the pension reviews transfer, a range of different solutions. People had experienced the same thing from different angles."

Figures to the end of 2014 show that the Guernsey regulator licensed 85 new international insurance entities last year, meaning there was a total of 797 international insurance entities domiciled in Guernsey at the end of 2014.

Further data showed that ILS was responsible for 45 percent of new business during the year.

Global reinsurer capital reaches $575 billion

Global reinsurer capital has risen to $575 billion, according to an Aon Benfield study.

The study estimated that global reinsurer capital rose 6 percent in 2014, including a 28 percent increase in alternative capital to $64 billion.

Capital reported by the 31 reinsurers surveyed rose by 2 percent to $346 billion, though the net income of $38.5 billion was offset by dividends and share buybacks of $22.3 billion.

Gross property and casualty premiums rose 2 percent to $198 billion, with reinsurance volume unchanged at $89 billion, despite the industry's pricing pressure.

Over the course of 2014, net catastrophe losses declined from 5.6 percent to 3.8 percent of net premium earned and were "well below" the long-term average, according to Aon Benfield.

Mike Van Slooten, head of Aon Benfield's international market analysis team, said: "Sector consolidation is underway as companies look to achieve the advantages of scale and diversification, one of the drivers being enhanced access to alternative capital."

"Three recently announced merger and acquisition transactions between [the companies surveyed] will reduce the number of entities in the study going forward."

The survey showed that reinsurers are now incorporating material alternative capital (through insurance-linked securities, sidecars and asset management mandates) to lower their cost of underwriting capital.

Bermuda targets Canadian firms

The Bermuda Business Development Agency (BDA) has teamed with local industry experts to create and host a webinar that highlights the benefits for Canadian firms of setting up insurance companies in the domicile.

"This is our first BDA webinar, and it demonstrates the value of our public-private partnership—we really appreciate the voluntary work of our industry partners on this project to heighten the visibility of Bermuda's captive insurance business," said BDA business development manager Jereme Ramsay.

"Our end goal is to help create new captive formations on the island. This particular webinar is aimed at CFOs and risk managers at companies in Canada, where we are working to develop new business in the insurance sector."

Canadian interest in Bermuda as an international business centre, particularly for establishing captives, has increased since the Canada-Bermuda Tax Information and Exchange Agreement (TIEA) took effect in 2011, putting the island on an equal tax footing with jurisdictions that hold tax treaties with Canada.

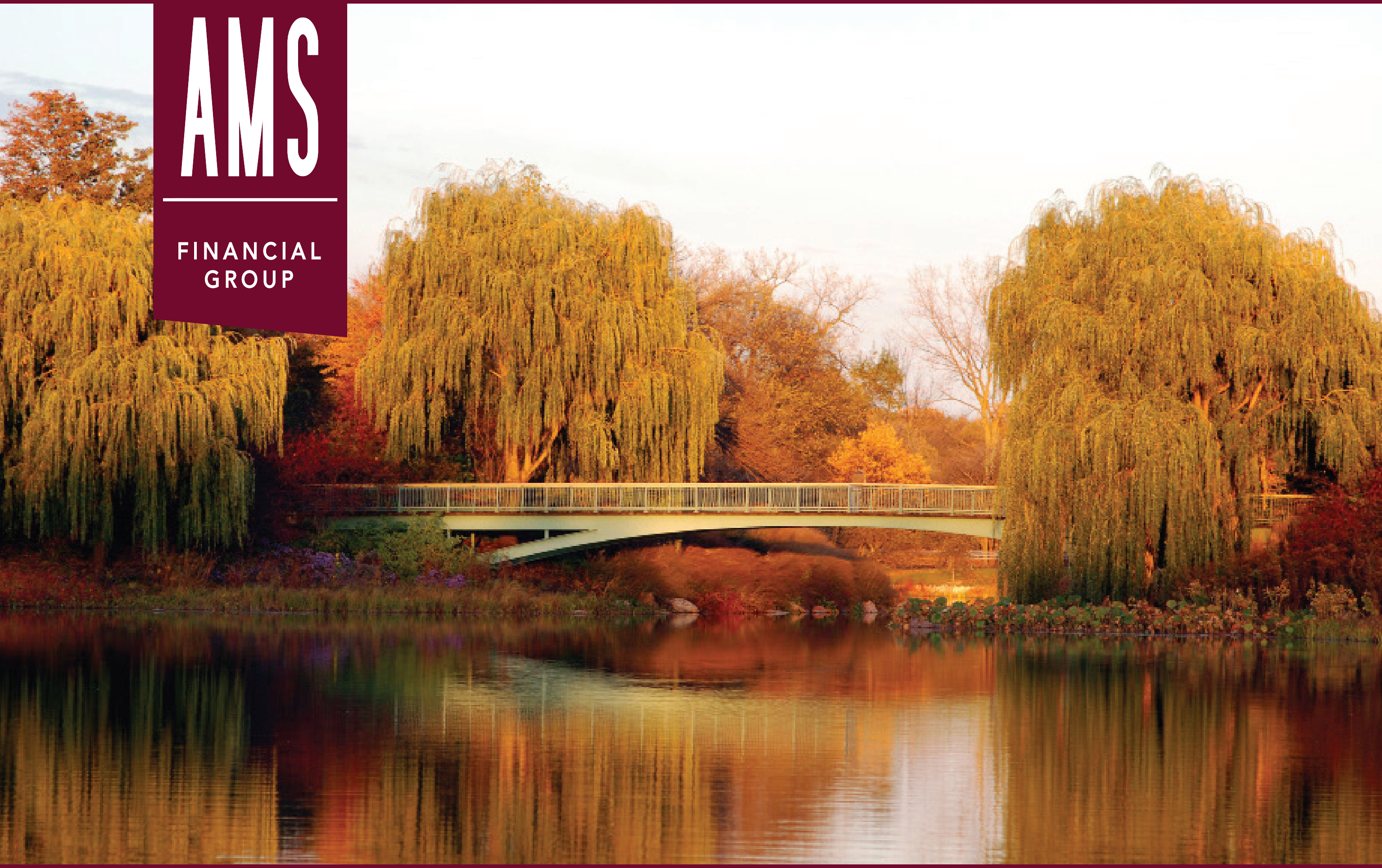
The bilateral agreement allows Bermuda insurance subsidiaries of certain Canadian corporations with international operations to be eligible for Canadian tax benefits, including the tax-free repatriation of certain dividends to Canada.

The BDA webinar will guide registrants through what a captive is, as well as common structures, reasons for setting up a captive, Bermuda's regulation and licensing process for captives, as well as provide an overview of Canadian income tax considerations.

"We have an excellent panel of experts lined up for this event," commented Joe DaSilveira, senior vice president at Liberty Mutual Management.

"The webinar is a must for any Canadian executive curious or thinking about forming a captive."

The BDA plans to stage at least three more webinars on risk industry topics this year—targeting US, Latin American and healthcare sector audiences—building towards scheduled events and business development roadshows.


AMS
FINANCIAL
GROUP

"Webinars are an effective platform to reach a broad global audience with our message about Bermuda's benefits," added Ramsay.

"We believe webinars will be a cost-effective way to generate leads and educate overseas companies and executives about the value of Bermuda to their business."

DaSilveira will moderate the discussion, while Oceana Yates, vice president of captives for R&Q Quest Management Services; Leslie Robinson, assistant director of corporate authorisations for the Bermuda Monetary Authority; and Mark Allitt, director of KPMG Advisory Limited, will also feature.

A.M. Best affirms National Grid captive

A.M. Best has affirmed the financial strength rating of "A (Excellent)" and the issuer credit rating of "a" of National Grid Insurance Company (NGICL) from the Isle of Man, a captive of National Grid. The outlook for both ratings remains stable.

The ratings reflect what A.M Best called NGICL's "very strong" risk-adjusted capitalisation, as well as its importance as a risk management tool within the National Grid group. A partially offsetting factor is the potential earnings volatility inherent in the captive's book of business.

The agency stated that NGICL's risk-adjusted capitalisation is expected to remain very strong, supported by internal capital generation.

In addition, there has been a reduction in underwriting risk, following the decision by the National Grid group in August 2014 to cease ceding its US business to NGICL and instead cede this business to a separate and newly incorporated US domiciled captive.

NGICL retains some exposure to US risks through a layer of stop-loss reinsurance protection provided to the new US captive.

The captive remains core to National Grid's risk management strategy, despite the reduction in US business.

It is "well integrated" into the parent's overall risk management framework, according to the agency, with its primary objective to mitigate the National Grid group's exposure to property damage and business interruption risks.

Prospective underwriting performance is likely to remain volatile, owing to the nature of underwritten risks. The captive is exposed to potentially large losses on its property and business interruption account.

However, technical performance over the long term has been "good", said A.M Best, demonstrated by a five-year average combined ratio of 65 percent.

The impact of large losses on the captive's balance sheet is partly mitigated by extensive reinsurance in place with a panel of financially strong counterparties.

A.M. Best said that negative rating actions may occur if there were material deterioration in NGICL's risk-adjusted capitalisation or a prolonged period of poor operating results.

If the captive's importance as a risk management tool within the National Grid group were to diminish, there may be negative rating pressure.

SCCIA request NAIC clarification

The South Carolina Captive Insurance Association (SCCIA) has requested assistance with the National Association of Insurance Commissioners staff proposal to change the definition of a multi-state reinsurer.

The SSCIA's Michael Coulter has requested in writing that the new proposed preamble to the Part A: Laws and Regulations accreditation standards are clarified to the extent that the Captive Life/Health Reinsurers section is the only section of the preamble applicable to captive insurers.

Coulter said: "The language in the Life/Health and Property/Casualty Insurers section of the preamble does not exclude captive insurers, and the language in the Captive Life/Health

Reinsurers section does not provide that the captive insurers described in that section are the only captives to which accreditation standards apply."

As many captive insurers write property/casualty coverage, the SCCIA is concerned that the absence of clarifying language in the Life/Health and Property/Casualty Insurers section of the preamble could be interpreted to apply to captive insurers.

In the letter, Coulter claimed that such an interpretation would be "disastrous" for the captive insurance industry.

He continued: "We respectfully request that you add suitable language to the preamble clarifying that captives are not subject to the Part A accreditation standards."

The SCCIA said that the following, or similar language, in the Life/Health and Property/Casualty Insurers section of the preamble could be used: "For avoidance of doubt, in no event shall Part A standards apply to any captive insurers other than those captive insurers described under the Captive Life/Health Reinsurers heading."

Smaller companies driving growth

Smaller insurance companies in both emerging and developed markets are the main engines of growth, according to a report from A.M. Best.

It states that, in mature markets, these companies tend to operate in specialised niches of unique expertise while companies in emerging markets, regardless of size, compete in all segments and businesses.

However, the benefits of being larger are not only evident in the economies of scale, which result in lower combined ratios, but also in the dependency on investment yields and reinsurance.

A.M. Best studied more than 1,900 insurers across four geographical groupings, examining results from 2007 to 2012 to compare market dynamics, drivers of profitability and balance sheet composition for companies in each region studied.

The regions studied were: mature markets, represented in this study by France, Germany and the UK; Brazil, Russia, India and China; the Middle East and North Africa (MENA); and Mexico, Indonesia, Nigeria and Turkey.

According to the report, emerging markets have shown much faster compound annual growth rates over the past decade than the mature ones—a range of 12 percent to 20 percent, versus around 4 percent.

Emerging markets have insurance penetration of less than 4 percent, measured as the ratio of premiums to GDP, while in developed markets the same ratio exceeds 7 percent—a far greater untapped potential relative to the size of their economies, according to A.M. Best.

Vasilis Katsipis, general manager of market development for MENA and South and Central Asia, said: "While the global economic crisis produced an outright shrinkage in gross written premium in the mature markets, the effect in the emerging markets was only a temporary slowdown in the rate of expansion."

"In the MENA region, growth weathered not only the economic slowdown but the social and political upheaval of the Arab Spring."

The report also discussed the drivers of profitability in the different regions. In this area, Mahesh Mistry, director of analytics, noted how the relationship between companies' size and performance begins to diverge between mature and emerging markets.

Mistry said: "In mature markets, small companies hold some distinct advantages, particularly in their underwriting performance, which tends to be marked by good claims ratios."

"Large companies [usually] have good claims ratios when there is [a] low frequency of large claims or no catastrophic activity impacting their results, and mid-size companies tend to have the highest claims ratios in their markets and combined ratios that seldom dropped below 100 percent in the period examined."

"Claims ratios in emerging markets tend to be in the same groupings as those observed in the developed markets, thereby dispelling the belief that claims ratios in emerging markets tend to be several percentage points better than those in developed markets."

ACE to offer clinical trials liability

ACE Group has launched an enhanced clinical trials liability proposition, which provides life science companies with specialist insurance for clinical trials programmes conducted anywhere in the world.

ACE Clinical Trials has been developed to offer timely and compliant cover as well as flexible solutions equally suitable for single trials and for large multinational trial programmes.

It is designed with pharma manufacturers, biotech organisations, medical device and equipment makers, generics companies, and research organisations in mind.

One of the main benefits of this increased cover is the introduction of fronting for large captive clinical trials programmes.

It will offer global casualty cover, including for the US, for UK-based life sciences companies, through ACE's network and team of specialist life science and liability underwriters.

The cover will also have a flexible capacity of up to $75 million aggregated limit available per investigational product.

Mark Roberts, casualty manager for the UK and Ireland at ACE, said: "ACE Clinical Trials is another example of how ACE brings its specialist expertise and global experience to meet the needs of businesses."

"With the experience of Claire Wilkinson, our in-house clinical trials expert based here in the UK and the strength of the ACE network of offices in 54 countries, clients can rest assured that their programmes will be compliant wherever they may be taking place," added Roberts.

"Clinical trials are a key stage in the development of medicinal products and providing compliant cover and quick turnarounds ultimately benefits both patients and companies."

Strong ratings for Energas

A.M. Best has affirmed the financial strength rating of "A (Excellent)" and the issuer credit rating of "a" of Energas Insurance of Malaysia. The outlook for both ratings is stable.

According to the agency, Energas's ratings reflect its strong capitalisation, comprehensive reinsurance protection and role as the sole captive insurance carrier for its ultimate parent, Petroliam Nasional Berhad (Petronas), an integrated global oil and gas company.

Full profit retention in the absence of dividend payments to Petronas has enabled Energas to grow its capital favorably since inception.

Energas's financial performance is underpinned by its low operating cost structure and consistent investment profits.

Energas has a large investment portfolio comprising of solely cash and cash equivalents, providing a high level of liquidity and minimum investment risk exposure. Its comprehensive reinsurance programme from a panel of high quality reinsurers limits Energas's aggregate loss exposure.

Offsetting rating factors include claims volatility from a narrow scope of assumed risk and increased event retention, especially as premium rates in its main engineering line remain soft while insured values are increasing.

A.M. Best said that negative rating actions may arise from a material deterioration of Energas's risk-adjusted capitalisation due to a material repatriation of capital.

Strong FSR for PCH Mutual

The Financial Stability Rating (FSR) of "A, Exceptional", assigned to PCH Mutual Insurance Company, a risk retention group (RRG), has been affirmed by Demotech.

This level of FSR is assigned to insurers that possess "exceptional financial stability" related to maintaining positive surplus as regards policyholders, liquidity of invested assets, an "acceptable" level of financial leverage, "reasonable" loss and loss adjustment expense reserves and "realistic" pricing.

Demotech's FSRs summarise its opinion of the financial stability of an insurer, regardless of general economic conditions or the phase of the underwriting cycle.

FSRs utilise statutory financial data based on insurance accounting principles prescribed or permitted by the National Association of Insurance Commissioners.

PCH Mutual was formed in 2004 by a group of personal care homes in Pennsylvania in response to the need for a segregation of insurance for adult residential care facilities that do not provide skilled care.

Facilities such as these include personal care homes, assisted living facilities, adult foster care, adult family homes and other similar types of operations.

The RRG is currently writing various limits of liability insurance in 37 states.

Domiciled in Washington DC, PCH Mutual's programme management is provided by PCALIC out of central Pennsylvania.

Heritage gains Lloyd's status

Heritage Insurance has gained Lloyd's registered broker status.

Having this status allows Heritage Insurance Solutions, the Financial Conduct Authority-regulated arm of the Guernsey-headquartered Heritage Group, to place business directly with Lloyd's underwriters.

Lloyd's is the global centre for specialist insurance and reinsurance and an international broker market, where underwriters come together as syndicates to insure risks.

Heritage Insurance Solutions managing director Karl Bradley said that becoming a Lloyd's registered broker was a significant boost to the firm's global insurance offering.

"Lloyd's is recognised as the leading market for both UK-based and international insurance risks. With our expertise and enhanced ability to provide a range of insurance for our clients we are excited about the new opportunities that our direct access to Lloyd's underwriters brings."

Bradley added that gaining Lloyds's registered broker status has been part of a longer term strategic aim of developing the insurance intermediary client offering within the Heritage Group.

"Financial risks clients in particular, in both the UK and offshore jurisdictions, will see immediate benefits from this development both in terms of a wider market offering and a closer Lloyd's market working relationship," he said.

Moving with the times

Willis Re has highlighted the need for change across the reinsurance industry as it forms a "new paradigm".

According to Willis Re's latest report, reinsurers are seeking to implement major changes to their strategies and business models to accommodate the growing transparency of major buyers around their core partner strategies,

Mergers and acquisitions (M&A) activity among reinsurers also continues to gather pace, according to Willis Re, with three major transactions announced since 1 January 2015.

With the pool of potential partners shrinking, Willis Re claimed that aspiring consolidators are now increasingly concerned about missing out on what many observe to be industry change that could last across generations.

The report also highlighted that insurance-linked securities (ILS) funds are not immune to current market challenges.

Reduced returns and the downward pressure on fees are placing the business models of some smaller standalone ILS managers under duress, explained the report.

Peter Hearn, global chairman of Willis Re, said: "ILS fund managers evolving into more traditional reinsurer models and reinsurers expanding their own fund management activities appear best placed to trade through this difficult period; they can manage investors and access business more effectively."

"But while this convergence trend is both logical and anticipated, it is creating a conundrum: as ILS funds evolve their business models to look more like traditional reinsurers, they are diluting the differentiation of the very offering which has proved so attractive to date for major primary buyers."

John Cavanagh, global CEO of Willis Re, added: "The April 2015 renewal season has reinforced current trends and the market continues to favour the buyer."

He claimed diversification is now the "key competitive advantage" in the reinsurance industry, and the ability to deliver a differentiated service offering is critical.

Hamilton Insurance acquires Sportscover and Kinetic

Hamilton Insurance Group has completed the acquisition of Sportscover Underwriting, a Lloyd's managing agent that manages Syndicate 3334, and Kinetic Insurance Brokers, a Lloyd's insurance broker.

Former CEO of Torus's International Operations, Dermot O'Donohoe, has been approved as CEO of the managing agency, now known as Hamilton Underwriting.

O'Donohoe's approval follows an announcement in January that signalled Hamilton's intention to appoint the Lloyd's underwriter to lead the development of the company's operations at Lloyd's, pending approvals.

Syndicate 3334 will use the brand name Hamilton at Lloyd's in marketing and other communications materials.

Kinetic will retain its name but will be branded as "A Member of the Hamilton Insurance Group" going forward.

The completion of the transaction follows Hamilton's announcement in November 2014 that it had entered into a deal with Wild Goose Holdings, the Australian-based holding company for the Sportscover group, to acquire Sportscover's managing agency and Kinetic.

The transaction between Hamilton and Sportscover required the approval of Lloyd's, the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA).

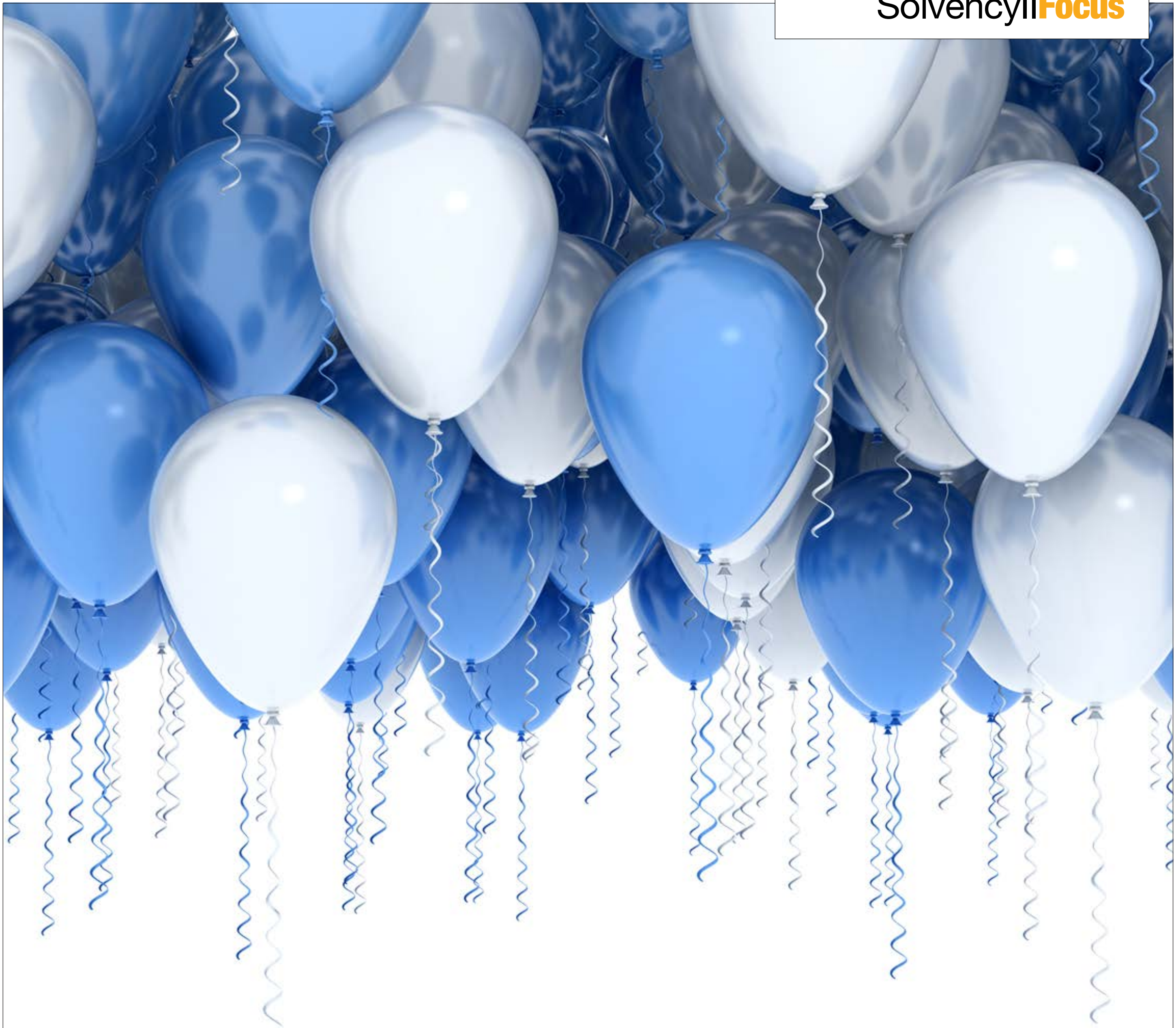
Together, Hamilton and Wild Goose have provided Funds at Lloyd's for the 2015 year of account.

Hamilton CEO Brian Duperreault said: "Since we established our company just over a year ago, gaining a presence at Lloyd's has been a key strategic initiative as it offers a well-recognised international platform."

"Through our operations in Bermuda, the US and now at Lloyd's, we are able to support profitable growth and expansion on a worldwide basis," he added.

"We would like to extend our appreciation to Lloyd's, the PRA and the FCA for the guidance they provided throughout this process and for its positive outcome."

Tweeting on Twitter? So is @CITimes



Benefits for all

It goes without saying that the introduction of Solvency II has brought with it great challenges for insurers. But ECIROA chief Günter Dröse feels the way forward is to work together, and keep things simple

STEPHEN DURHAM REPORTS

In your opinion, how ready are Europe's captive insurers for the arrival of Solvency II?

As far as I understand, all of Europe's insurers are currently preparing themselves for implementation in January 2016. The bigger captive managers such as Aon, Marsh and Willis all have structures in place and an idea of how to fulfil all of the requirements. On the other hand, the smaller, self-managed entities from many countries will have asked their particular regulators' advice on how to manage certain aspects of the requirements.

The key factor is that each country will have its own approach to how they deal with the Solvency II requirements themselves. Either way, all of them are 100 percent aware of it and no one is in danger of being caught sleeping. It is important to remember that implementation is a flowing situation. Some countries demand more from their insurance companies, including captives, and others demand less.

What are the main advantages and disadvantages for insurers that are preparing to comply with Solvency II?

There are no real difficulties to speak of. There might be different adjustment needs in different countries. We have data on 130 captives in Europe, collected parallel to the quantitative impact study (known as QIS 5) exercise based on the expected Solvency II rules, many of which have different strategies.

In Luxembourg, for example, it is a must to establish high reserves, which means there is always enough liquidity to pay out. In Ireland however, an insurer cannot immediately pay out of its own assets and so has to get the money paid by someone who has issued a letter of credit and pay them back via its parent company.

So we see, even under the existing framework, that different countries have had different ways of dealing with the requirements under Solvency I. Despite this, I would not see a problem for either of the countries I mentioned in adjusting to Solvency II. Any problem a domicile had would have most likely been present prior to Solvency II. A well-managed captive will easily survive.

In terms of advantages, there might be a flight into diversity. In other words, companies may begin trying to write more business on lines of insurance besides the traditional property and casualty, to get additional benefits.

This reduces the need for capital, as the diverse lines are more balanced. I would like to think that the future for European captives is bright and only those who are either very small or do not have the proper loss ratio will struggle.

How much demand do you think there will be from the captive industry for the assistance of service providers such as BNP Paribas to aid with reporting?

In the market there are a lot of companies offering to support captives in establishing a proper Solvency II structure. In truth, I don't know how much they will be used by captives following implementation. The majority of self-managed captives will seek out an actuary or an external auditor as they need them.

With Pillar III requirements, they may need a proper reporting tool, but in each and every country captives are only a small piece of the cake. Service providers offer this kind of assistance to all mid-sized and smaller insurers that do not have internal services and may need some help. I think most are too expensive and it could be reasonable, over time, to do these things by yourself.

How is Solvency II expected to affect other, non-European, domiciles in terms of gaining equivalence?

The International Association of Insurance Supervisors (IAIS) is currently developing standard capital requirements by itself and has rolled out a proposal for cross-border groups and local supervisors to comment on. The European Insurance and Occupational Pensions Authority (EIOPA) wanted to influence this as much as possible, as it believes Solvency II is the one and only such set of requirements.

The relationship between Europe and the rest of the world is difficult. For the time being, I wouldn't comment on other domiciles. EIOPA's phrasing excludes captives in its opinions of other countries such as Bermuda, so does that mean the rules are not equivalent? EIOPA does not specifically say that, it just carves out any mention altogether. The problem is whether insurance and reinsurance contracts between domiciles such as Bermuda and companies in Europe will be affected.

Another strange point is that EIOPA does not fight with the National Association of Insurance Commissioners in the US about what is the right or wrong approach. It is flexible to the point where it has a problem. So it allows itself judgement on Japan, Switzerland or Bermuda, but not on the US.

Are there any problems with Solvency II that are still in need of ironing out prior to implementation?

It is very important that Solvency II looks as if it will be more challenging for insurers than capital requirements are for banks or financial institutions. Although insurers are unlikely to see an additional burden, it still seems unfair that financial institutions do not have to underpin each and every risk with capital.

The banks are happy so they will not discuss it. In the insurance market, however, each and every type of risk has to be underpinned and so the burden is higher. I believe there is a need to review these requirements, less the insurance market become strangled.

It is a matter of fact that today, and in the near future, Pillar III will require insurers to publish all of their data, but this will not lead to any additional transparency.

It will make rating agencies, accountants, analysts, consumers and whoever else is in charge of assessment more puzzled than ever before. Data in Pillar III is often contradictory to Pillar I or the company's balance sheet.

In essence, five different sets of data are presented and it is difficult to understand if they are consistent. Worse still, there is nobody in the market who knows why this is. This is the opposite of transparency, and has been implemented not for consumer protection but for their own protection if an insurer fails.

It is a very peculiar situation, but the way forward is to work together, not to complicate things for each other, and hopefully it will work to the benefit of all. CIT

> "In the insurance market, each and every type of risk has to be underpinned and so the burden is higher. I believe there is a need to review these requirements, less the insurance market become strangled"

Günter Dröse
Chairman
European Captive Insurance and Reinsurance Owners' Association

Fiscally attracted to EU

Experts discuss where European captives are with Solvency II, and how they are adapting to today's financial environment

Dominic Wheatley
Chief executive
Guernsey Finance

Marian Fenton
Regional director of Europe and Bermuda captive services
AIG Global Risk Solutions

George Mangion
Senior partner
PKF Malta Accountants & Business Advisers

William Dalziel
Partner and head of institutional clients
London & Capital

Lorraine Stack
Business development leader EMEA and Asia Pacific
Marsh Captive Solutions Group

Stephen Durham
Reporter
Captive Insurance Times

What challenges do European captives currently face in the run-up to Solvency II's implementation next year?

Dominic Wheatley: Captives domiciled within the EU will have to comply with Solvency II's blanket approach to the regulation of insurance and reinsurance business. It is designed to deal with problems within the commercial market and therefore some of the requirements are simply disproportionately onerous for captives.

George Mangion: Preparation for Solvency II has been on the forefront of all regulatory activity during 2014 and will continue to be so in 2015. Solvency II may, under certain circumstances, call for higher capital requirements, enhanced governance and internal control procedures, and additional supervisory and public disclosure.

Solvency II is expected to increase consumer protection and establish more transparency for supervisors and investors. Nevertheless, the majority of Maltese captives serve a specific corporate risk financing and management purpose in the interest of the group of companies for whose benefit they have been established.

Therefore, generally pure captives (that is those that do not write third-party business) have another purposes. Under Solvency II, captives are will have to re-evaluate the use of their capital and explore new investment opportunities, among other things. This will inevitably lead to the incurrence of additional costs. Insurers have to prepare and disclose detailed quantitative reports to be in compliance with Pillar III, most of which will be of a technical nature and hence, require additional expertise.

Against this backdrop, PKF Malta is currently carrying out a survey among Maltese insurers (including captives and reinsurers). The survey shall recognise the major changes that companies had to undergo to follow Pillar II and III requirements, and ultimately to assess whether the proportionality principle applies to Maltese insurers. The survey results shall be delivered on 21 May 2015 at the 8th Annual Conference of Finance Malta.

William Dalziel: Solvency II is set to change the regulatory landscape for insurers in Europe. Between the requirements of the three pillars, insurers have been undergoing a top-to-bottom review of their capital management, risk modelling and analytical frameworks. The new regulations present challenges from an underwriting, reserving and investment perspective as they have been designed to ensure that insurers have sufficient capital to withstand adverse events, both in terms of insurance risk, and also economic, market and operational risk.

From an investment perspective, the new regulation will impose changes on portfolio modelling, construction and reporting that captives need to start addressing no later than Q3 2015. Aspects to be considered under Solvency II include:

- Impact of asset capital weighting on asset allocation and portfolio modelling;
- Availability and granularity of portfolio data; and
- Risk governance.

Solvency II's capital weighting model assigned to different asset classes may mean some insurers will need to set aside additional capital to allow for certain investments in their current portfolios. These capital weights will be imposed on securities based on factors such as asset classes, credit rating and duration.

There is, therefore, a pressing need for captives to review their current portfolios to get a clear understanding of the impact of these changes on their expected returns on a capital-adjusted basis. Going forward, this will require performing capital-adjusted expected returns and volatilities, which minimise unrewarded risk and therefore optimise the use of the Insurer's capital.

The use of currency and duration matching, together with capital-weighted prospective asset returns and volatilities will be required to establish optimal asset allocations in the context of capital efficiency.

Governance is a key theme throughout Solvency II. The underlying rationale of the legislation is to ensure insurers fully grasp the risk in their organisation. Therefore, captives will need to continually review market risk factors and, where appropriate, apply risk budgets to ensure the investment portfolio serves their business, not the other way around.

Lorraine Stack: The majority of European captives are deep into Solvency II implementation and are in a strong position to meet the requirements of the new regime in 2016. Many had already implemented some of the governance and risk management aspects of the directive prior to 2014, so when the European Insurance and Occupational Pensions Authority (EIOPA) interim guidelines were introduced, these companies were ready to focus on the solvency requirement and the completion of the Forward Looking Assessment of Own Risk (FLAOR). The FLAOR exercise has allowed captive boards to see the alignment of Pillars I and II and the resulting impact on the Solvency Capital Requirement charge. In doing so, the process has improved risk awareness and the ability to manage risk more efficiently.

Many captives are now addressing issues that may have been identified in the FLAOR exercise for 2014, and are completing any outstanding governance and risk management policy documentation.

An issue on the horizon for captives is the area of regulatory reporting or the Pillar III aspects of the directive. Certain technical areas of the reporting process may present challenges for some captives. It remains to be seen if the principle of proportionality will be applied to captives in this area. Potential solutions are being worked upon and test reporting is being conducted in some domiciles this year.

Marian Fenton: Although Guernsey is not in the EU (it is in Europe geographically) and as such, is not required to implement Solvency II, the island is updating its own risk-based, proportionate solvency regime in line with the Insurance Core Principles of the International Association of Insurance Supervisors.

The challenges of Solvency II are in achieving the appropriate balance between increased governance and reporting requirements and captives' essential nature as lower risk entities within the overall European regulatory universe.

For the captive community, proportionality is a key principle in the application of Solvency II as it allows the requirements to be applied in a manner that is proportionate to the nature, scale and complexity of the business.

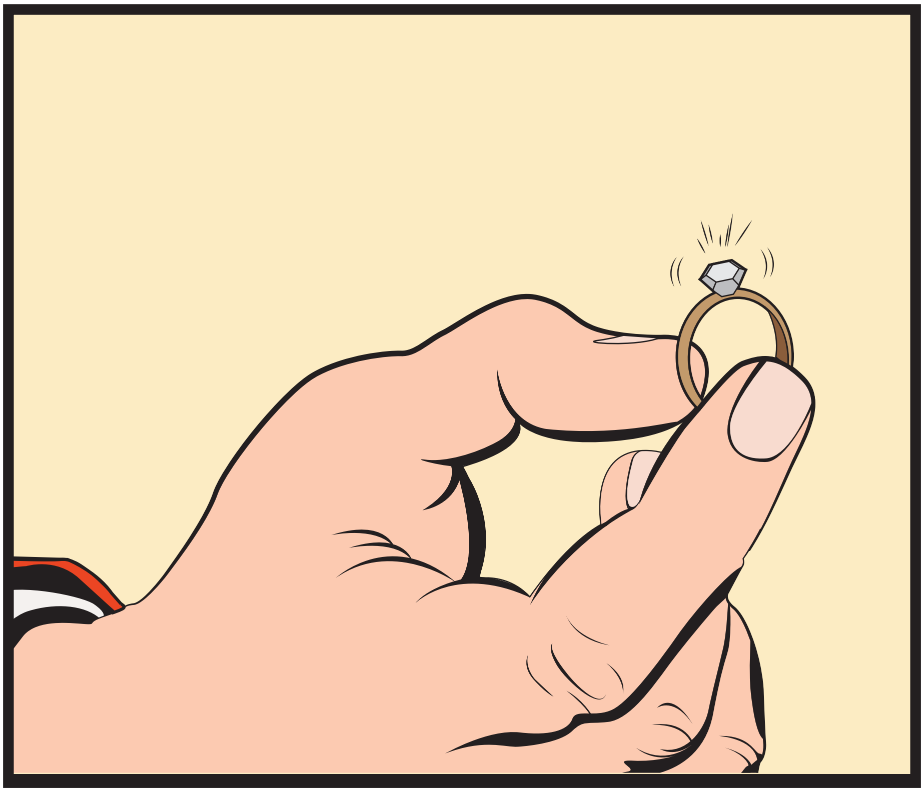
Captive mangers play a pivotal role in supporting the captive board of directors, and the parent company in achieving a proportional, fit-for-purpose approach.

The additional costs, resource and time requirements of this transition to the new regulatory framework do present challenges for captive budgets and have led to an examination of the strategic benefits that a captive delivers for the parent group.

However, periodic strategic reviews of a subsidiary's contribution to the wider group are a feature of modern economic life and a captive is no different in that respect. In fact, this type of examination is healthy and can identify new ways in which the captive can be utilised and remain relevant to the group's overall goals.

How will Solvency II's capital requirements affect funding—will the cost be too high for captive owners, or do they already have this in the bag?

Mangion: Malta is adopting the principle of proportionality for captive insurers. Malta's captive managers are remarkably positive about Solvency II, perhaps because the end is in sight, and they and their clients have, in effect, done all the hard work. Solvency II will not only address insurance risk, but instead it will take into consideration a wider spectrum of risks when calculating capital requirements. A challenged faced by most of captive owners was whether they will opt for the internal model versus the standard formula to calculate the minimum solvency requirements.



Captives have done the necessary tests and are poised for the changeover. Captive owners are confident that they have surpassed the learning curve and are now in the implementation period and shall reap the benefits of their thorough preparation. The common perception is that there is now a well-developed expertise in the cost-effective application of Solvency II to suit particular clients' needs.

Furthermore, the concept of risk-based supervision is spreading beyond the EU, so one hope that other offshore domiciles like Guernsey will be playing catch-up with the onshore EU domiciles.

Stack: The first real indication of the directive's capital requirements came with the fifth quantitative impact Study, conducted in late 2010. This exercise flagged anomalies, where captives with certain risk structures incurred large capital charges. However, the majority of captive results produced realistic capital requirements and captive owners have had time to meet the requirements in the lead up to introduction of the directive.

Capital requirements under Solvency II are more complex and may indeed present challenges to entry for smaller companies, with the exception of those that were already in run-off, we have not seen captives closing or moving away from EU domiciles due to Solvency II. In fact, the certainty around Solvency II had a positive effect on recent formation activity across EU domiciles in 2014. We expect this trend to continue in 2015.

Fenton: Captives tend to be conservative by nature, not just because of the regulatory framework that they operate in but in the very real sense they are an investment of the parent's money, resources and time. For this reason captives have always been cautious investors of capital funds. The advent of Solvency II causes captives to look at their capital needs through a new lens and to understand the financial implications of decisions around investment counterparty selection and diversification.

Through the forward-looking Own Risk and Solvency Assessment, captive owners and managers are gaining a better understanding of the capital cost implications of management decisions around areas such as:

- Underwriting risk selection;
- Loans/funds advanced to group companies;
- Counterparty selection (both investment and reinsurance);
- Diversification; and
- Risk mitigation.

Where the initial results of this assessment in the 2014/2015 preparatory phase have highlighted issues for individual captives, they are actively looking at how they can alter aspects of their structure to get greater capital relief in a cost efficient manner.

Wheatley: All captives based in the EU will have to comply with Solvency II's requirement for insurance and reinsurance companies to hold sufficient capital to meet their obligations over the next 12 months with a 99.5 percent confidence level. This is unnecessarily burdensome for captives and may even render some captive business plans uneconomic and unviable.

Unlike Solvency II, Guernsey's new regime distinguishes between commercial insurance, reinsurance and captive insurance. As such, captives in Guernsey will have a minimum capital requirement of £100,000 and confidence levels of 90 percent. This proportionate approach should be very attractive to current and potential captive owners and especially those who still want a domicile within the European region.

How are European captive owners managing their capital in a difficult economic environment?

Stack: Generally speaking, it's difficult to measure the impact of the economic environment on the captive sector. However, it is clear that captive owners remained fully committed to the use of their captive throughout the economic downturn.

The captive played a critical role in the insurance and risk management aspects of the businesses and owners continued full compliance with solvency requirements. We do not believe that maintaining capital at the appropriate level has been an issue.

Overall Solvency II will provide increased flexibility around captive investment strategy and many companies are revisiting investment strategy to potentially reduce Solvency II capital requirement. Also, companies are looking at potentially more efficient sources of capital, such as ancillary own funds. Where a parent is highly rated (BBB and higher), intercompany lending back to the parent can be very favourable from group perspective and provides an option which was not as broadly or consistently available under the Solvency I regime.

Fenton: Captives, like other group subsidiaries, are expected to deliver value from their capital funds. The added challenge for captives is that they must do so in full conformity with the regulatory environment in which they operate. In many cases, cash flow benefits through intergroup cash pooling facilities provide the best use of funds to the group as returns on many low-risk investments are almost negligible.

The key is in achieving a balance from a solvency capital perspective as such arrangements can carry a significant capital charge for counterparty default risk especially within an unrated group.

As captive owners and managers become more familiar with the sensitivities within the standard model, they can best see how to diversify the management of capital funds.

Dalziel: The current economic environment, in combination with impending Solvency II regulation, will present challenges ahead for European insurers.

From an investment perspective, insurers have been altering the composition of their portfolios to maximise their capital-weighted returns. In the current low-yield environment there has been a tendency to increase exposure to higher-yielding, higher risk investments. However, with the impending Solvency II regulation, this tendency needs to be considered in tandem with the trade-off of increasing the amount of required capital. Only those businesses that enjoy a reasonably 'fat' level of shareholders' excess reserves may continue to run with these capital-hungry assets.

The regulation will impose capital weights on securities based on factors such as asset classes, credit rating and duration. Captives should consider reviewing their current portfolios to get a clear understanding of the impact of these changes on their expected returns on a capital-adjusted basis.

These types of considerations have resulted in many insurers reducing their portfolios' allocation to capital-intensive investments, such as asset-backed securities and long-dated high-yield bonds. There has been the major shift out of equities as they not only present a volatile return prospect but have a significant capital weighting under Solvency II regulation, rendering them inefficient on a capital-adjusted basis.

Elsewhere, insurers have been increasing their allocation to investments that are less capital intensive, such as shorter-dated investment grade bonds and mortgage bonds. In many cases more capital is being allocated to government/sovereign bonds, which may not incur a capital charge, even with the current low-yield environment. From an accounting perspective, despite investments earning near record low yields, the valuation of the captive's liabilities should move broadly in line the valuation of the investments, as the discount rates are also near record lows.

With that said, one of the consequences of Solvency II is the temptation to 'manage the model' rather than manage the market. The best approach in the current environment therefore is to actively manage risk exposures in response to evolving macro-economic conditions, all the while taking into account regulatory demands.

Mangion: In the midst of this concern of higher capital requirements and costs associated with satisfying all the requirements under the Solvency II framework. European captive owners should ensure that they work with insurance partners that appreciate the potentially significant increase in the capital and compliance requirements imposed on them by Solvency II. Maltese captives were required to conduct a during 2014 and submit the report to the Malta Financial Services Authority before 31 December 2014.

The captive insurance industry has a long tradition of evolving and innovating to serve changing needs and new industries. For

many the challenge brought by Solvency II is to see the wood for the trees. Last year was the year catastrophe bonds and insurance-linked securities (ILS) were taken to a new level. Catastrophe bonds have grown extensively, and now play a central role in market for catastrophic risk. It is not expected that catastrophe bonds and ILS will replace reinsurance but acts as complement to the reinsurance market. Malta is now the only state in the EU with cell legislation for issuers of ILS. It is targeting the ILS, catastrophe bond and reinsurance convergence sector.

Wheatley: The new solvency regimes are pushing up the capital requirements for captives. However, this is restricted to secured assets and yet they are low yielding.

As such, this is squeezing the margins for captives and therefore this undermines their economic viability especially in the context of soft conventional insurance units. In Guernsey, captives are addressing this by upstreaming to parents as a way to decrease the counterparty risk and enhance returns.

Which captive structures are proving the most popular in Europe, and why?

Wheatley: There were 85 new international insurance entities established in Guernsey during 2014. Some of these were established using limited companies but the vast majority were protected cell companies (PCCs) and incorporated cell companies (ICCs) and related cells.

Guernsey pioneered the concept when it introduced the PCC in 1997 and therefore has built up significant experience and expertise in using cell companies within the captive insurance sector. In the last year we have seen a number of captive insurers established as ICCs to transfer pension longevity risk.

For example, BT's pension scheme has established a new insurance company, BTPS Insurance ICC, and enabled the transfer of a quarter of the scheme's exposure to increased longevity and so hedged around $16 billion of liabilities. Similar structures have since been established by Towers Watson and PricewaterhouseCoopers to facilitate transactions for their pension fund clients.

The ability to quickly and cheaply establish new cells is a major reason for the popularity of PCCs and ICCs and is behind their use within Guernsey's fast-growing ILS market and the collateralised reinsurance segment.

This has been enhanced by the fact that protected cells conducting collateralised reinsurance business are able to secure regulatory pre-authorisation. Guernsey's regime has now been enhanced further by the publication of guidance notes on the use of transformer vehicles for insurance and reinsurance business.

Stack: The traditional single parent direct or reinsurance structure is still the most popular captive arrangement. However, we are seeing interest in alternative structures such as PCCs and special purpose vehicles. The evolution of the captive model into these non-traditional structures essentially makes captives more accessible for small- and mid-sized companies as well as large organisations.

We are also seeing growth in captive participation in multinational employee benefit financing arrangements, with several employee benefit captive programmes currently being contemplated or implemented in a number of domiciles.

Captive usage in defined benefit pension financing arrangements is also a trending area; although most defined benefit pension plans are closed, many companies still face significant challenges in the management of legacy obligations. We expect to see further innovation involving captive structures in the pension area going forward.

There also continues to be growing interest in the use of captives to insure trade credit, customer warranty programmes, and cyber risk coverage.

Mangion: The PCC structure is one of the most popular structures for captives. Malta is the only EU country offering PCCs. A European captive gives insurers the opportunity to write insurance business for which they have been authorised throughout the EU under the European passport rights. The most important advantage of the PCC model is that an individual cell may carry out insurance business through a certain cell without having to go by the own funds requirements, through using the cell company's core capital. In addition, cellular assets that are contained in one cell are only available to meet the liabilities of that specific cell.

This results in the concept of segregating cellular creditors, meaning that cellular creditors contracting with the PCC in respect of a particular cell only have a right of recourse against the assets of that cell. Typically though, creditors of a cell may also have the right to secondary recourse to the core assets of the PCC, with the condition that the cellular assets of that particular cell to which the liability is associated with have been used up fully.

A cell of a PCC does not have separate legal personality, and as a result, under the quantitative capital requirements of Pillar II, a cell will typically need to put up its own funds equivalent to the calculation of the cell's notional solvency capital requirement. In addition, a PCC has the possibility to produce a single own risk solvency assessment for the entire PCC. The same applies to Pillar III reporting and disclosure requirements.

Fenton: We are seeing a greater focus on reinsurance captives utilising net retention programmes and moving away from the structure of accepting gross risk and ceding this via the captive to the market or a non-European group captive. This change in strategy comes about as captives look to minimise their counterparty default and

operational risk exposures and associated capital costs in the Solvency II environment.

The compliance cost of operating a direct writing captive is also an area that we see companies critically assessing and in some cases the fronted solution provides greater value taking into account the risk retention needs and geographical risk distribution of the parent.

What are European companies considering before they launch a captive? How has the reasoning behind formation changed in the years following the crisis?

Mangion: The financial crisis of 2008 showed significant exposures in the insurance sector. Political, regulatory and financial uncertainty affected insurance market pricing, reinsurance level, investment policies and capital requirements.

In its aftermath, regulators and insurers have devoted considerable effort to better understanding insurance risks. For many years, a number of multinational enterprises have embraced the opportunity to operate their own captive insurance company. Most of which were established to offer insurance coverage in circumstances where cover was unavailable or unreasonably priced.

In fact, industries such as construction, manufacturing as well as professional services regularly face industry-specific risks exclude general liability insurance, errors and omissions policies, as well as reputation risks. In the last decade, small- to medium-sized companies have also learned that the captive insurance entities can provide them significant benefits, which include attractive risk management elements, asset protection from the claims of business and personal creditors, access to the lower-cost reinsurance market and insuring risks that would otherwise be uninsurable.

A properly structured and managed captive insurance company could provide various other tax savings opportunities.

In addition, the premium paid by the parent company can be invested and the return would be reserved and used in the event of a major future loss. Malta is well represented by a number of financial institutions, including well-recognised insurance managers and companies. Nevertheless, Malta continued to experience a healthy increase in captive business, particularly originating from some of the largest blue chip corporations.

Malta's captive insurance industry has the potential of growing with good reputation, an approachable and motivated regulator and a strong financial sector.

Wheatley: Captives might be established for a number of reasons, including the insurance of unusual risks not catered for by the commercial market or where market capacity is limited, direct access to reinsurance markets, paying premiums related to the insured's own track record and the retention of net premiums over claims.

However, the financial crisis highlighted major failures of corporate governance and has brought about increased focus within the boardroom on de-risking companies.

Establishing a captive improves the understanding of risk and the cost of risk management within a company and as such has been a major driver in the continued use of captives within Europe. Yet, the use of captives in Europe has not reached such deep penetration as in the US and this suggests that there is scope for further growth.

I would expect the number of formations to continue to build across Europe as a result of current trends in corporate governance and risk financing technology. The trend being seen across many major companies is for the retention of larger and more complex risks, which need to be effectively managed from both a governance and financing perspective.

This results partly from the limitations of the conventional insurance markets and partly from the increasing willingness of companies to retain risk as a result of the deeper understanding of their own risk that arises out of the enhanced analytics and improved financial modelling available today.

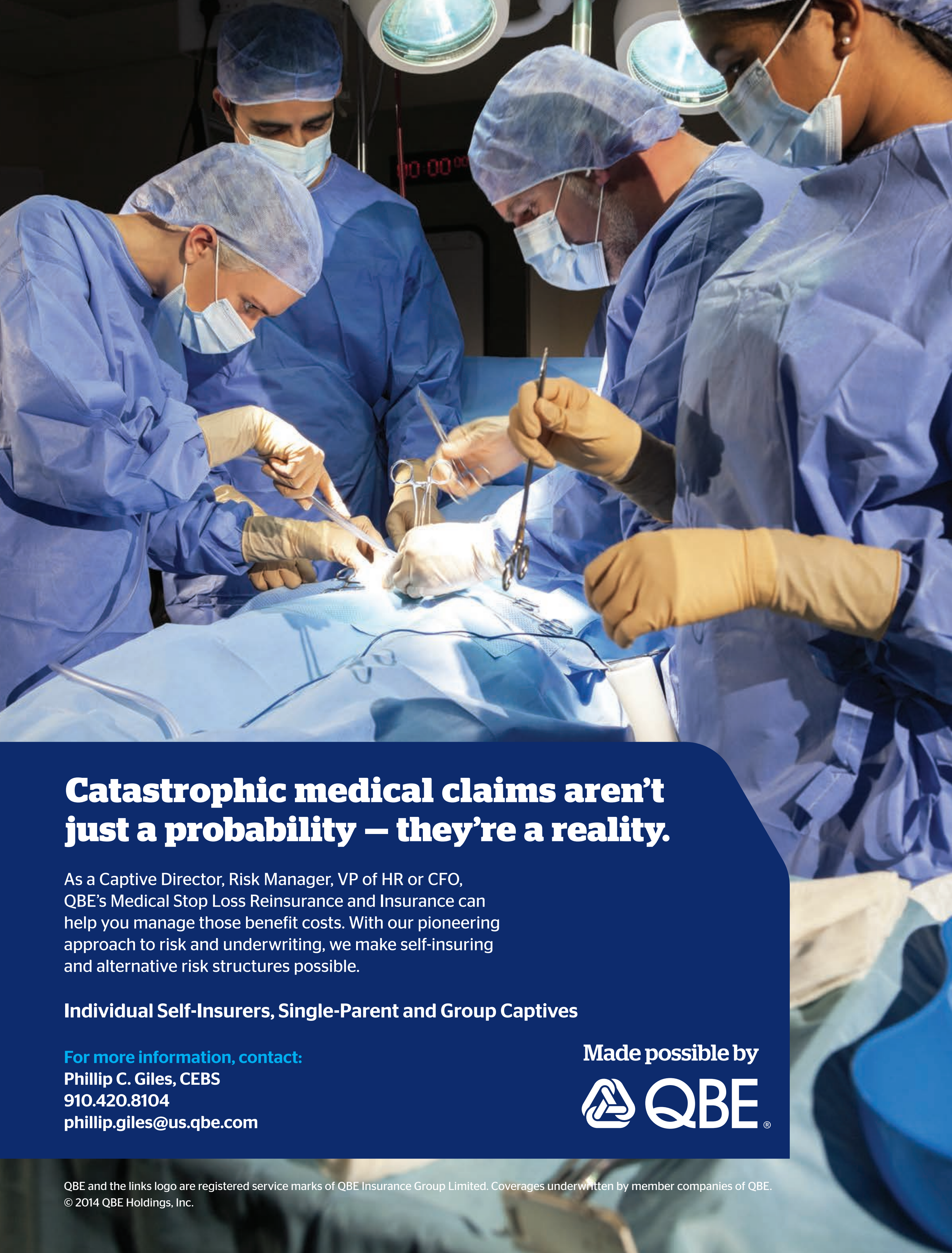
Stack: The areas of consideration in captive formation have not changed in the years since the financial crisis, and still include the assessment of the appropriate level of risk retention and most appropriate captive structure and domicile, a cost benefit analysis, and an assessment of capital, legal and tax issues.

What does appear to be changing is the level of sophistication with which these assessments are being made, increasingly involving the use of analytics to guide strategic risk planning. There is also a marked increase in interest around diversification of the captive model outside the traditional spheres of property and casualty, into non-traditional areas such as employee benefits as mentioned earlier. The captive option is increasingly being viewed as an enterprise risk management tool, which in turn has broadened the bandwidth of those in the assessment process, often including hands on involvement of stakeholders in finance and HR.

Fenton: The value proposition for a captive is now very firmly at the root of any decision making exercise. The feasibility exercise that companies carry out prior to launching a captive is now subject to greater challenges from the relevant stakeholders and a captive proposition must be able to demonstrably deliver true benefit via:

- Savings through risk management efficiencies; and/or
- Lower total cost of risk.

Prior to the financial crisis, the potential of investment return on funds maintained within the captive may have been a strong motivator, but in the current economic environment that is no longer a persuasive factor. **CIT**


Catastrophic medical claims aren't just a probability — they're a reality.
As a Captive Director, Risk Manager, VP of HR or CFO, QBE's Medical Stop Loss Reinsurance and Insurance can help you manage those benefit costs. With our pioneering approach to risk and underwriting, we make self-insuring and alternative risk structures possible.
Individual Self-Insurers, Single-Parent and Group Captives
For more information, contact:
Phillip C. Giles, CEBS
910.420.8104
phillip.giles@us.qbe.com
Made possible by
QBE®
QBE and the links logo are registered service marks of QBE Insurance Group Limited. Coverages underwritten by member companies of QBE.
© 2014 QBE Holdings, Inc.

The pick of the bunch

As one of only two domiciles that can offer both EU solvency standards and PCC cell solutions, Gibraltar prides itself on acting as the low-cost solution. Aon's James Clayton-Wright reports

The subject on the minds of most owners of EU based captives is Solvency II now that we are in the run up to full implementation in less than nine months.

With a soft market backdrop, Solvency II may additionally challenge some of the benefits offered by captives and so when considering where to establish a captive, corporations that have historically considered various jurisdictions' based on their regulatory regime, capital and fiscal requirements will need to factor in the additional requirements in place in an EU domicile under Solvency II. That said, when we look at the bigger picture, especially in view of the International Association of Insurance Supervisors (IAIS) Core Principles and those broader regulation changes on the global horizon, of which Solvency II forms a part, it is clear that a risk-based approach to capital with a more sophisticated but proportionate approach to governance and risk management is where insurance regulation is headed.

Ultimately, this can only be beneficial for the industry.

In light of this changing landscape, Aon has developed innovative approaches in order to assist our captive clients prepare for Solvency II implementation. The first solution for our Gibraltar-based captive clients was driven by a regulatory reporting deadline of 31 December 2014 for submission of completed Forward Looking Assessment of Own Risk (FLAOR) reports.

Part of our solution under Pillar I was to also tackle the Solvency II standard capital requirement formula calculation at the same time as the FLAOR, which required a large volume of input data and numerous individual calculations, some of which are iterative in nature. To help our clients calculate their

Solvency II Pillar I requirements Aon has developed Astra, which is an Excel-based Solvency II standard formula tool. This is a simple, easy to use and cost effective solution to completing the standard formula calculation, which we were able to use to help our clients prepare and submit their FLAOR on time to the Gibraltar regulator, the Financial Services Commission (FSC).

The next challenge comes in the form of governance requirements under Pillar II as captives are also required to adopt a comprehensive and documented formal risk-based governance framework. Aon developed an integrated and online governance, risk management and compliance (GRC) system to help our clients address these requirements.

Our GRC platform provides consistency at all levels and avoids extensive documentation of policies and procedures. Furthermore, our GRC platform helps our clients avoid complex and uncontrollable implementation programmes, whilst maintaining a structured approach across all organisational levels with a fit for purpose cost efficient solution.

Finally, we have Pillar III, which will play a key role in the Solvency II regime by promoting market discipline and encouraging greater transparency between firms, the regulator and the public. The new reporting regime will consist of two types of report:

- The Solvency and Financial Condition Report—this is public; and
- The Regular Supervisory Report—this is a private report between a firm and the regulator and requires information to be collated and submitted by way of quantitative reporting templates.

These new requirements constitute a significant change to the current reporting regime, both in terms of content and frequency. As such, Pillar III is potentially the most onerous of the three pillars with regard to the level of information required. Aon is developing a quantitative reporting tool designed to streamline the quarterly and annual reporting obligations under Pillar III. This software will link into various Aon systems including Astra and the GRC in order to further ease the reporting requirements our clients now face.

We expect that with the solutions we have and plan to put in place to meet the requirements of Solvency II in the EU and the IAIS Core Principles beyond the EU, our clients will continue to achieve the value a captive solution can bring. However, we are also mindful of how this evolving regulatory landscape may cause a reassessment of current and future captive arrangements.

One trend that is starting to emerge is the increased use of cells in protected cell companies (PCCs), both for new clients and some existing captive owners.

In the past some EU and non-EU parent companies formed direct writing captives to facilitate fronting their EU-based risks to their non-EU domiciled captive. Solvency II will impact this structure going forward as it is driving the need for large capital increases to cover both captives' statutory requirements along with the duplicated administrative cost and time.

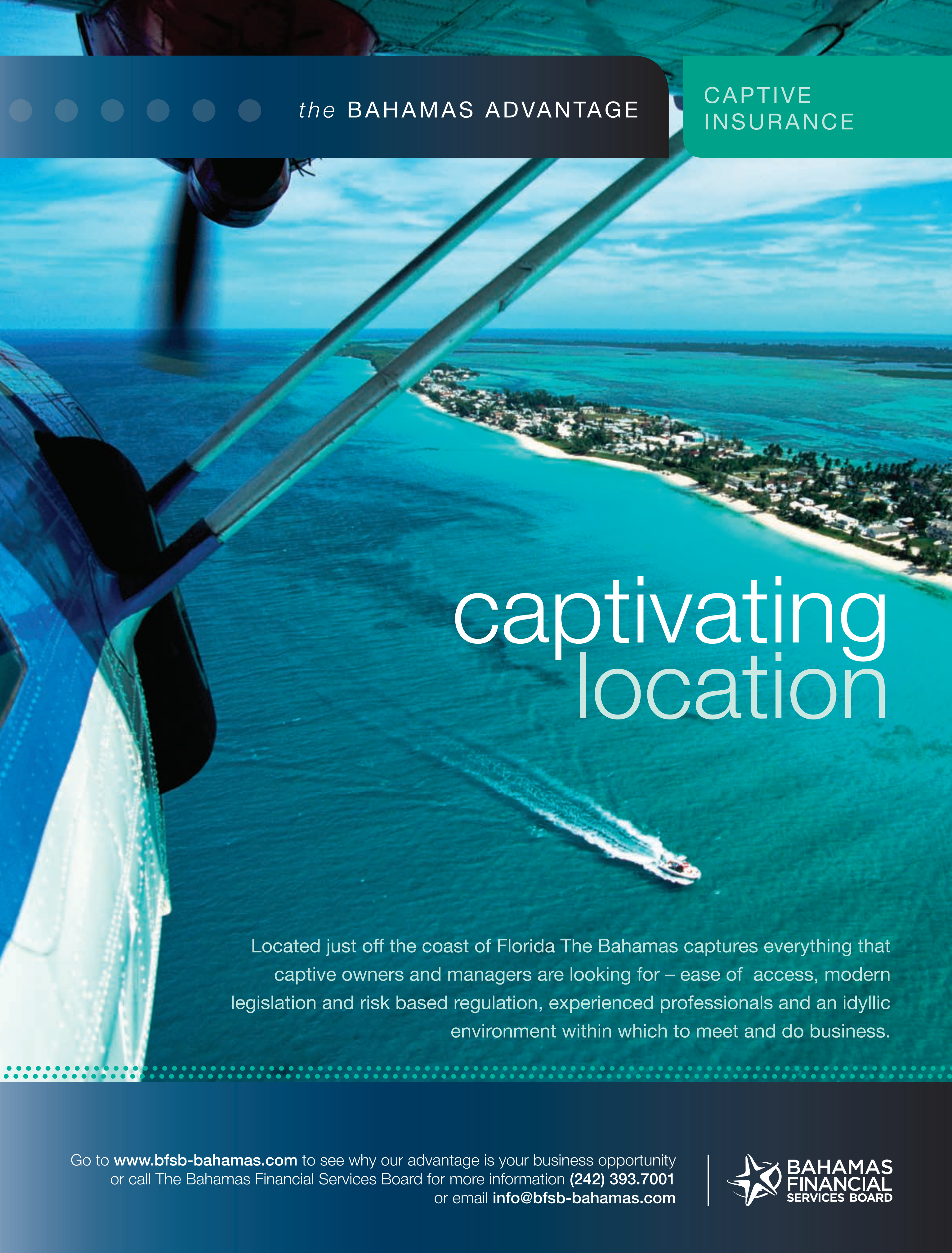
In these cases, a PCC alternative may help and an advantage for our clients is that Gibraltar is well placed to assist due to its PCC legislation. Aon is able to provide various solution options through Aon-owned White Rock Insurance (Gibraltar) PCC, (the oldest established PCC in the EU).

Another area that is getting increasing attention is mergers and acquisitions (M&A). Past M&A activity has left some global parent companies with multiple captives, current renewals are now falling into the new legislation and owners are realising the operating and capital inefficiencies that remain in their existing strategies. We are seeing an increased interest in Gibraltar as a location to facilitate the warehousing of these multiple captive reserves into cells and then reinsuring to the main risk taking captive. This allows the release of excess capital and the rationalisation of the number of standalone captives in the group.

As Solvency II has compelled organisations and their risk management departments to re-assess their captive strategies, it has also triggered entities to consider their retention strategies, and this is where Gibraltar's regulatory environment, including PCC solutions, is a major differentiator.

As one of only two domiciles that can offer both EU solvency standards and PCC cell solutions, Gibraltar can offer companies with a lower premium spend that want some of the gains of risk retention management without the associated capital and management costs. **CIT**

James Clayton-Wright
Insurance manager
Aon Insurance Managers (Gibraltar)


the BAHAMAS ADVANTAGE
CAPTIVE INSURANCE
captivating location
Located just off the coast of Florida The Bahamas captures everything that captive owners and managers are looking for – ease of access, modern legislation and risk based regulation, experienced professionals and an idyllic environment within which to meet and do business.
Go to www.bfsb-bahamas.com to see why our advantage is your business opportunity or call The Bahamas Financial Services Board for more information (242) 393.7001 or email info@bfsb-bahamas.com
BAHAMAS FINANCIAL SERVICES BOARD

They did it their way

The doors of Nevada's captive insurance industry have been open for some time, and they are staying that way

STEPHEN DURHAM REPORTS

With more than a decade of captive experience under its belt, Nevada is one of the more flexible locations in the captive industry. This is best demonstrated by the Nevada Division of Insurance, which offers a dedicated captive team, low captive application expenses, simplified annual financial reporting for pure captives, and a 24-hour verbal approval for a completed pure captive application.

Ellen Charnley, global sales and marketing leader of the captive solutions division at Marsh, adds: "The dedicated captive team work closely with captive managers and parent companies during the application process to ensure the formation goes as smoothly and efficiently as possible."

"Finally, the division has established a captive advisory council consisting of owners and service providers that meet formally two times per year to discuss the Nevada captive environment."

Where the captive division has demonstrated its flexibility is the licensing of risk retention groups (RRGs). Neveda initially, during the early 2000s, focused on pure captives, though it introduced a number of agency captives and then eventually RRGs.

Nevada is currently the biggest RRG domicile outside of Vermont and has more than 25 registered RRGs, which account for a 15-percent share of its total captive base.

Despite the state's strong performance in RRGs, it took the surprise decision to suspend licensing of RRGs to give the captive division time to catch up with growth rates and build what it referred to as an "appropriate" infrastructure.

At the 2014 captive advisory council meeting, the captive division said the domicile was again ready for RRGs and would welcome any applications that may see fit to domicile in the state.

Robert Vogel, vice president at Pro Group, says: "Nevada has developed a seasoned regulatory staff that is business friendly. Sound experienced regulation is paramount in the captive industry and Nevada offers that."

"The captive industry is supported by all levels of the state government including the governor's office. Additionally, travel to and from Nevada is very convenient and is an obviously popular destination location."

The presence of experienced regulators is a testament to the way in which Nevada is determined to make waves in the captive industry, despite its age and competition. A key facet of this is its focus on regulation.

Mike Lynch, the deputy commissioner at the Nevada Division of Insurance, says: "Nevada's refined corporate laws allow for optimal use of a captive programme. It is a priority to take a progressive approach and revolutionise our regulatory framework to meet the needs of the growing captive insurance market."

"Nevada is working with the National Association of Insurance Commissioners (NAIC) on the recently proposed amendment to the accreditation standards preamble that could have unintended consequences for captive insurers. Nevada is also working with the NAIC and our congressional delegation to draft proposals for the bill which may eliminate the 831(b) tax exemption for traditionally structured captive insurers."

Nevada's captive insurance programme outperformed its growth and speed expectations by approving 26 captives in 2014, resulting in a captive premium increase to $3.8 billion.

The state's insurance commissioner Scott Kipper said, following the results, that 2014 was once again a record breaking year for the Nevada captive insurance industry. Nevada now has 160 domestic captive insurers.

"As one of our nation's oldest and largest captive domiciles, Nevada prides itself on its ability to maintain consistent and high regulatory standards, while also providing good service and a business friendly regulatory environment," said Kipper.

Nevada now offers regulatory options for captive formations including series limited liability companies (LLCs) and segregated cell captive programmes.

In recent times, the state has seen rapid growth in captive utilisation by new segments, including biotech, alternative energy, transportation and manufacturing, as well as growth in captives for financial institutions.

"We saw a lot of companies choose to take advantage of Nevada's efficient application approval and series LLC legislation," said deputy commissioner Michael Lynch. "After another record breaking year, it is obvious that business owners worldwide consider Nevada to be a leader as a captive domicile."

Nevada has licensed more than 200 captive insurers since the inception of its captive insurance programme in 1999.

Charnley continues: "For Nevada, their ease and flexibility of doing business has led to their increased growth rates and I would anticipate these rates continue as Nevada builds credibility and experience over some of the newer domiciles."

"Remember that Nevada has been a captive domicile for more than a decade, so it's now more established as a domicile when compared with some of the newer jurisdictions like Texas, North Carolina and Connecticut."

For the US, continued growth in the small captive segment seems almost essential, as organisations start to really get their arms around funding for risks that they actively choose to retain.

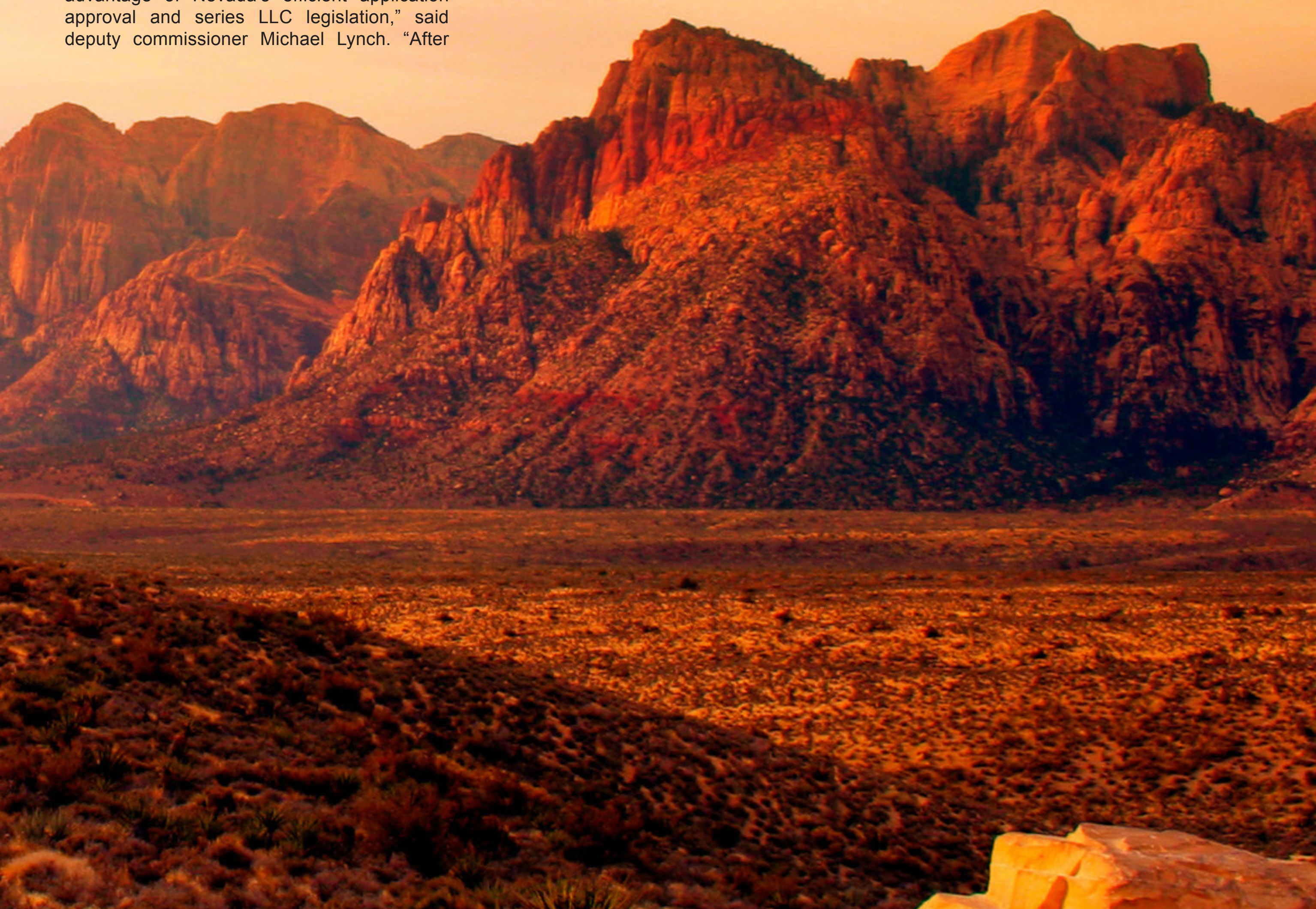
Charnley adds: "Worldwide, we anticipate growth in some of the new markets in Asia such as China and also Latin America. Captive growth in 2014 was over 7 percent over 2013 and the total captives worldwide was more than 6,870.

This industry continues to evolve and adapt to an ever changing environment and we will likely see continued growth into the future."

While captives as an alternative risk transfer mechanism have been around for centuries, in the last several decades, US onshore domiciles have embraced the benefits of captive insurance.

Charnley adds: "From multibillion dollar companies to smaller mid-market companies and non-profits, they are thriving onshore with their captive."

"The expansion of domiciles in the US provides companies more options depending on the type of captive wherein they can gauge regulator specialties and make informed decisions on which domicile is best for them and their business. Nevada's doors are open and have been for many years." **CIT**



Missouri's family values

Maria Sheffield explains how Missouri takes care of its own

STEPHEN DURHAM REPORTS

How has Missouri fared in terms of captive insurance growth in the past six months? Are there any new strategies in the pipeline for 2015/16?

In Missouri, we believe that the overall health of our captive industry is more important than the number of captives we license each year. We believe steady growth and sustainability is the key to a successful captive programme.

Our captives are subsidiaries of some very noteworthy industry leaders and are generating billions of dollars of premium volume as a result.

I joined the Missouri Department of Insurance about 18 months ago and we have licensed 20 new captives in that time. Quality is the key to long-term success. Our goal is to set a standard of excellence and attract first-rate, superior captive business, and therefore we do not set specific targets. That being said, we do have a desire to responsibly continue the growth our captive programme.

How supportive is Missouri's government to its captive insurance industry?

Missouri appreciates the opportunities for economic development within the captive industry and dedicates the resources necessary to support its success. In fact, Missouri's captive insurance law includes a dedicated funding mechanism so we can maintain our experienced staff, bring in new technical talent as needed, and continue to manage all aspects of our captive insurance programme without the need for outsourcing.

> "Our focus is on creating a sound and solid captive regulatory environment that serves as an asset to companies doing business in the state"

We also maintain offices in St Louis, Kansas City and Jefferson City, and we use those offices to ease the burden for out-of-state travellers who are interested in forming a captive in the State of Missouri.

Are there any regulatory changes coming up for the state in 2015?

We do not have immediate plans to make any revisions to our captive insurance laws as those we have in place now are working well for our state, however, we continue significant outreach to the captive community. We are always interested in hearing proposals and ideas as we work with those in the captive industry to develop new solutions.

Generally, we continue to focus on solvency modernisation initiatives that are important to both the captive insurance industry and the insurance industry at large.

With the IRS increasing its scrutiny of micro captives, does this concern a state as established as Missouri?

We have not structured our captive programme in Missouri in such a way that we focus on or favour any specific type of captive structure or line of business. We consider every captive applicant on the merits of its application and carefully review every captive application to ensure compliance with our laws and regulations. We have captives writing anywhere from one line of coverage up to 20 lines of coverage.

Missouri captives are formed to mitigate exposure to a wide range of risks.

Practically every risk underwritten by a commercial insurer can be provided by a Missouri captive. The majority of our captives provide mainstream property/casualty insurance coverage such as general liability, product liability, workers' compensation deductible, director and officer liability, errors and omissions liability, auto liability and professional liability. Some of our captives also provide specialised coverage for unusual or hard-to-insure risks.

Here, our focus is on creating a sound and solid captive regulatory environment that serves as an asset to companies doing business in the state of Missouri. We do this by being both responsible and responsive to the needs of the business community and the captive industry in our state. We provide prudent and balanced regulatory oversight of each licensed captive for the most favourable long-term effect on the captive industry.

How important is solvency in a Missouri captive? Is the state making any steps towards equivalence with Solvency II jurisdictions in Europe?

One of our primary responsibilities as insurance regulators is ensuring the solvency of the companies we regulate. The globalisation of insurance makes it clear that insurance supervisors around the world need to provide well-defined and unambiguous guidance to afford the financial system with a pillar of stability and consumers with peace of mind.

The role of insurance supervisors has never been more critical. It is my belief they need to work with present supervisory systems rather than thinking new globalised standards can be used to dramatically reshape those established under existing law.

As we move forward on solvency issues, practical and implementable change should be evolutionary, not revolutionary. Further, the work done by insurance supervisors must be credible, and it therefore must be transparent. Transparency is critically important in developing the national and global response to financial stability.

As insurance regulators, it is important to recognise the specific nature of the insurer and the risks posed. The most efficient supervisory regime tailors its approach so that policyholders are protected and financial stability is maintained, without applying regulation that, with regard to the nature of the company, is unnecessary and may hinder the efficiency of the market.

Insurance supervisors should take the necessary time to develop standards appropriate to the insurance industry, and resist the pressure to homogenise regulation to treat all products the same.

It should be well recognised that confidence in the integrity of insurance regulation must be maintained in order to ensure the viability of the industry.

Is the state continuing to educate the industry?

Missouri hosted its own captive insurance conference in the autumn of last year and will play host to the Western Region Captive Insurance Conference in May.

We devote a significant portion of our time to meeting with not only companies that are interested in forming a captive in Missouri, but also the various service providers in the industry, including actuaries, accountants, lawyers, agents and brokers.

One of our primary marketing objectives is to provide networking and educational opportunities for our captive owners to facilitate captive growth in Missouri. CIT

Maria Sheffield
Captive programme manager
Missouri Department of Insurance

Industry Events

16th Annual SCCIA Executive Educational Conference

Location: South Carolina
Date: 21-23 September 2015
www.sccia.org

Save the date for the 16th Annual SCCIA Conference, returning to downtown Charleston September 21-23 2015. The event features presentations by the top players in the industry, continuing education opportunities, networking and fun.

35th Annual National Educational Conference & Expo

Location: Washington DC
Date: 18-20 October 2015
www.siia.org

SIIA's National Educational Conference & Expo is the world's largest event dedicated exclusively to the self-insurance/alternative risk transfer industry. Registrants will enjoy a cutting-edge educational program combined with unique networking opportunities, and a world-class tradeshow of industry product and service providers guaranteed to provide exceptional value in three fastpaced, activity-packed days.


HELP TAKE CARE OF YOUR PEOPLE AND BUSINESS TOGETHER.
With Zurich, you can get a variety of tailored global solutions: employee benefits, liability and property insurance. And if you consolidate them into a single captive it could be financially beneficial – giving you greater control of your insurance portfolio.
FIND OUT MORE AT zurich.com/captives
ZURICH INSURANCE.
FOR THOSE WHO TRULY LOVE THEIR BUSINESS.
ZURICH®

Industry appointments

Willis Group Holdings has appointment **Marc Paasch** as global head of alternative risk transfer (ART) solutions.

Paasch joins Willis from Marsh, where he was a managing director, head of analytics and co-head of risk consulting in Europe, as well as a member of the Marsh France executive committee.

Prior to that, he held senior management positions in the financial services sector in Paris and New York, including at Allianz and Société Générale.

ART solutions enable businesses to transfer traditionally uninsurable risks to a third-party balance sheet and with Paasch it will further bolster Willis's ability to deliver risk solutions.

Paasch will report to John Merkovsky, Willis's global head of risk and analytics, who commented: "The addition of Paasch to our risk and analytics team will enable Willis to leverage the risk insights gained through our cutting-edge analytics to deliver alternative techniques to hedge and transfer risk."

Insurance manager Robus and Hexagon Protected Cell Company have appointed two new directors in Guernsey after strong company growth.

Jamie Polson and **Ben Dunning** join from Aon Insurance Managers.

Polson will serve as the client lead on a portfolio of insurance companies managed by Robus, with responsibility for his clients complying with all legal, regulatory, compliance and corporate governance requirements.

Dunning has joined Hexagon, which is owned by Robus, as group accountant and director.

In his new role, he will be responsible for reviewing accounts, auditing and ensuring that management agreements, regulatory and legal requirements are met.

Chris Le Conte, managing director of Robus Group, commented: 'The appointments of Polson and Dunning reflect the growth Robus has seen in recent years. Between them they have 30 years' experience in the captive insurance industry and are welcome additions to the board."

Jeremy Soames has resigned as chairman of Barbican Managing Agency (BMAL) after five years in the role.

During Soames's time as chairman, BMAL's stamp capacity grew from £180 to £260 million.

Richard Hobbs, who has moved from his current position as BMAL's senior independent non-executive director to become chairman, will take from the departing Soames. Hobbs previously held roles relating to the regulation of the insurance industry and, in particular, the Lloyd's market.

David Reeves, Barbican Group CEO, commented: "We thank Soames for his leadership and look forward to working with Hobbs, who we already know well, to take BMAL forward through the next phase of its development."

Liberty Speciality Markets (LSM), a part of Liberty Mutual Insurance Group, is to restructure its senior underwriting management team.

Sean Rocks, chief underwriting officer of its commercial division, resigned from LSM on 31 October. **Alan Telford**, who is currently LSM's chief underwriting officer financial lines, will take over from Rocks.

Telford will assume the title of chief underwriting officer for the commercial division on 1 April.

Matthew Moore, currently chief underwriting officer for specialty and reinsurance, will become group chief underwriting officer.

He will retain the specialty portion of his current role, but with the additional support of Peter Smith, who becomes active underwriter of Syndicate 4472, subject to Lloyd's approval.

Dieter Winkel has been named as chief underwriting officer for reinsurance.

Nick Metcalf, president and CEO of LSM, commented: "The fact that these are all internal appointments demonstrates the depth of our underwriting and leadership talent, highlighting the breadth of opportunities within LSM and the wider Liberty Group."

JLT Re has appointed **Ed Hochberg** as CEO of North America.

Hochberg was previously global head of analytics, banking and advisory at JLT Re having joined as part of the 2013 Towers Watson Re acquisition.

He will report to Mike Reynolds, who is global CEO of JLT Re.

Before joining Towers Watson in 2003, Hochberg was senior vice president of financial products for PMA Re.

Prior to this position, he spent time at PMA Capital Corporation and Deloitte & Touche. He also served on the board of directors of Cathedral Capital.

Hochberg will retain the responsibilities for his current role as global Head of analytics, banking and advisory until a replacement is appointed which is expected to be in the near future, according to JLT Re. **CIT**

CIT CAPTIVEINSURANCETIMES

Editor: Mark Dugdale
markdugdale@captiveinsurancetimes.com
Tel: +44 (0)208 663 9620

Reporter: Stephen Durham
stephendurham@captiveinsurancetimes.com
Tel: +44 (0)208 663 9622

Editorial assistant: Becky Butcher
beckybutcher@blackknightmedialtd.com
Tel: +44 (0)208 663 9621

Account manager: Joe Farrell
joefarrell@captiveinsurancetimes.com
Tel: +44 (0)208 663 9627

Designer and marketing: John Savage
johnsavage@captiveinsurancetimes.com
Tel: +44 (0)208 663 9648

Publisher: Justin Lawson
justinlawson@captiveinsurancetimes.com
Tel: +44 (0)208 663 9628

Marketing director: Steven Lafferty

Published by Black Knight Media Ltd
Provident House, 6-20 Burrell Row
Beckenham, BR3 1AT, UK

Company reg: 0719464


Is your Manager listening?