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# CLEANING OUT MY CAPTIVE

## Fine-tuning the 831(b) election



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## RC Structures establishes new captive in Connecticut

RC Structures of Syosset, New York, is basing its captive insurance operations in Connecticut, the state's insurance department has revealed.

The new captive, RCX Insurance Company, is the tenth captive to be licensed in the state since 2011.

Janet Grace, programme manager for Connecticut's captive insurance division, said: "The department works with businesses of all disciplines and sizes to help control costs through the creation of captives that are well managed and sustainable."

"Our consultative approach to helping firms explore and license captives as part of strategic risk management is attracting businesses both in and outside Connecticut to domicile their captive here."

Jason Giessel, owner of RC Structures, added: "I feel very confident that our captive insurer will be a very effective management tool for our entire operation allowing us to remain competitive and grow our business."

## Better control needed for Solvency II

Insurers are complying with Solvency II but data is proving problematic, according to Craig Skinner, leader for insurance and investment management at PwC.

A review of insurers in the Internal Model Approval Process (IMAP), published by the Prudential Regulation Authority (PRA), was designed to assess the quality of data being used.

Skinner suggested that although insurers have made strides in complying with Solvency II, many are struggling to articulate, design and implement effective controls over material data.

He said: "Organisations are creating, collecting and storing ever-increasing amounts of more and more complex data."

"Coupled with the complexities of the processes and using multiple—and often legacy—IT systems, firms must apply ever more controls and ongoing assurance over material data in a pragmatic but rigorous manner."

He added that insurers that treat their data as a strategic asset could lay the foundations for achieving Solvency II compliance, as well as addressing other regulations and legislation.

He explained: "The General Data Privacy Regulation taking effect in 2018 will, on top of all the work completed to date regarding Solvency II, require firms to provide even more robust and transparent assurance over their data."

Yalini Pathy, leader of UK insurance investment management data governance at PwC, added: "The PRA findings are intrinsically linked and highlight the need for an effective data governance framework driven by bringing structure and consistency to an organisation's approach to data."

Pathy suggested that firms should consider design principles, making sure their solution is relevant and pragmatic, so that it can be successfully embedded.

She said: "Data governance, when pragmatically applied, does underpin wider commercial benefits. When data is protected and managed appropriately, there are benefits far broader than simple Solvency II compliance."

"The PRA findings complement our perspectives and experience, from supporting clients in the market, on the governance and controls that are to be applied to data used in the internal model."

## Flood Re secures £2.1 billion multi-year reinsurance programme

Flood Re has successfully secured a £2.1 billion multi-year reinsurance programme.

In an oversubscribed second phase of the tender process, Flood Re bound the additional capacity required to complete the placement.

The three-year reinsurance programme is one of the five largest natural peril reinsurance deals struck globally, and the second biggest in Europe, according to Flood Re.

The second phase saw 45 entities offer capacity to meet the required amount to complete the programme, with 38 of those parties securing a share of the placement.

During the first phase, which concluded in late 2015, several reinsurers collectively offered almost £1.29 billion of multi-year coverage, with Munich Re and Swiss Re both contributing significant support.

Brendan McCafferty, CEO of Flood Re, said: "Securing £2.1 billion in annual protection is an important milestone towards Flood Re being ready to accept policies for flood risk households."

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"Although the reinsurance process has now been completed on time and ahead of planned budget, there is still a lot of work to be done. We are testing our systems with insurers to ensure they work effectively and will also continue to work closely with the financial regulators to obtain the authorisation we need to operate."

The programme is a first in the UK for reinsurance cover under European Public Procurement regulations. It was conducted with the assistance of reinsurance broker Guy Carpenter.

Charles Whitmore, head of the property solutions group at Guy Carpenter, commented: "The reinsurance market has proved incredibly supportive of Flood Re from the outset, acknowledging both the opportunity and the level of professionalism running through the whole process. As a result, the final placement was relatively straightforward with the world's largest reinsurers providing the majority of the capacity."

### January weather causes \$4 billion global economic losses

January winter weather could cause up to \$4 billion of losses to the global economy, according to Aon Benfield's Impact Forecasting catastrophe report.

The report, Global Catastrophe Recap, which evaluates the impact of the natural disaster events, noted the powerful winter storm hit the US during the second half of January, killing 58 people and leaving dozens injured.

The report also noted that an Arctic cold snap meant snowfall covered much of East Asia, causing significant damage and killing 116 people across Taiwan, Thailand, Japan, South Korea and China.

Total combined economic losses from the event were cited at nearly \$2 billion, with China incurring \$1.6 billion of the total economic losses.

Adam Podlaha, head of Impact Forecasting, said: "Winter in the Northern Hemisphere was on full display to begin 2016, with several winter storm events impacting parts of the US, Asia and Europe."

"Despite winter weather historically not being one of the costliest perils when compared to tropical cyclones or flooding, these winter events can still pose billion-dollar costs to the global economy."

"The peril continues to be of interest to the insurance industry as claims resulting from heavy snow or ice often quickly accumulate."

### Captive Alternatives launches Puerto Rico captive

Captive Alternatives has launched a cell captive, Madison Re II, in Puerto Rico.

Madison Re II was formed to provide a new captive creation and management structure exclusively for Captive Alternatives clients.

The new structure will allow Captive Alternatives to quickly and efficiently create new protected cells, and provides additional opportunities for larger captives.

With the launch of Madison Re II, Captive Alternatives is consolidating all of its existing captives under management into Puerto Rico, making Madison Re II one of the largest insurance captive managers in the area.

According to Captive Alternatives, it elected to form Madison Re II in Puerto Rico because of the efficient, business-friendly atmosphere.

Mark Jacobs, president and CEO of Captive Alternatives, commented: "Establishing captives in Puerto Rico affords them the kind of security and flexibility they are looking for in a near-shore solution. It also allows us to offer clients an alternative solution, as Congress increasingly looks to change the 831(b) captive rules."

Alberto Bacó Bagué, secretary of economic development and commerce in Puerto Rico, added: "Captive Alternatives's decision to form Madison Re II in Puerto Rico is another vote of confidence from an international company with many choices for where to locate their operations."

### Cells dominate Guernsey business

Guernsey licensed 43 new protected cell company (PCC) cells in 2015, bringing the total to 444 for the year, according to the Guernsey Financial Services Commission (GFSC).

The domicile did lose 35 PCC cells in 2015, meaning a net change of eight, compared to 2014.

Guernsey also licensed three new incorporated cell company (ICC) cells, according to the GFSC figures, but lost two over the course of the year, bringing the total to 41 at the end of 2015.

Four ICCs were licenced and one departed, meaning that Guernsey was home to 41 of these captives by the end of the year.

Three new PCCs were approved by the end of 2015, but Guernsey also saw six departures, bringing the total number of PCCs to 64, compared to 67 in 2014.

Guernsey did not license any captives under the 'company' bracket during 2015, keeping its total at 242.

In total, Guernsey licensed 66 international insurers in 2015.

But it also saw 59 departures, meaning the domicile had 804 of these entities licensed at the end of the year.

Guernsey Finance CEO Dominic Wheatley said: "Confirmation that Guernsey ended last year with more than 800 international insurers is a terrific endorsement of our standing and expertise across the insurance sector."

"The island's excellent reputation in the London market ensures that much of our business originates in the UK, but insurers from all corners of the world are establishing in Guernsey."

The majority of the new insurance business in Guernsey, 44 percent, came from the UK, followed by business from the Cayman Islands, which accounted for 24 percent.

Insurance-linked securities made up the majority of business in 2015, at 38 percent, followed by property, which accounted for 14 percent of business.

Wheatley added: "The diversity of insurers choosing to establish here is testament to the professional environment in Guernsey."

"Guernsey offers the latest ... legislation, pragmatic regulation outside the Solvency II regime and a wealth of insurance management expertise; all of which are conducive to establishing an insurance business."

### Gateway Rivers and Palm Insurance complete merger

Gateway Rivers Insurance Company and Palm Insurance Company have completed their merger following AT&T's acquisition of TV satellite provider DIRECTV.

US telecoms company AT&T's Texas-domiciled captive, Gateway Rivers, received affirmations of its financial strength and credit ratings from A.M. Best after completion of its merger with DIRECTV's Hawaii-domiciled single-parent captive Palm Insurance.

AT&T completed its \$49 billion acquisition of DIRECTV in July 2015, creating the largest pay TV provider in the US.

According to A.M. Best, the affirmed ratings and outlook reflect Gateway's strong capitalisation, comprehensive risk management and favourable operating results, providing insurance coverage to subsidiaries of AT&T.



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Partially offsetting these positive rating factors are Gateway's exposure, although small, to Palm Insurance's unseasoned business, and Gateway's large limits on its property lines of business.

Despite the affirmations, Gateway Rivers, formed in 2014, has requested to be withdrawn from the A.M. Best rating process.

### Montana bags 38 new captives

Montana has continued its strong growth, licensing 38 new captive entities in 2015.

The 38 new captives licensed in 2015 included 32 pure captives, two dedicated-to-reinsurance captives, and four special-purpose captives.

John Jones, president of the Montana Captive Insurance Association, commented: "These latest numbers clearly demonstrate that Montana is serious about building a world-class captive insurance domicile."

The results revealed that, as of 31 December 2015, Montana had licensed a total of 191 standalone captive insurers and 307 total risk-bearing entities.

The 191 standalone captives were made up of 128 single parents, 28 for reinsurance, nine special-purpose captives, 16 risk retention groups, two association captives and eight protected cells.

Jones said: "We believe this success has been fostered through a combination of experienced and consistent regulators, supportive legislators ... and a highly effective industry trade association."



### SOBC acquires first Bermuda captive

SOBC Corp has completed its purchase of Insuratex, a Bermuda Class 3 captive in run-off.

This is the run-off acquisition and service specialist's first move into Bermuda and is in line with its stated intention to buy and service small or difficult legacy companies.

SOBC is able to acquire or manage marginally solvent insurance entities, books and lines of business, and to provide services for distressed entities that could be moving into run-off.

SOBC's management team noted that it looks forward to working in Bermuda, recognising the position the domicile holds in the captive insurance industry, the regulatory regime it follows and the specialist needs of its legacy sector.

Stephanie Mocatta, CEO of SOBC Corp, said: "We are really pleased to start 2016 with the acquisition of Insuratex."

"This acquisition helps to establish our base in Bermuda and allow us to look for other opportunities on the island. We will be managing the run-off of Insuratex in a professional and pro-active manner."

The acquisition comes shortly after JLT Towner Insurance Management's Thomas Hodson joined SOBC as general counsel.

### Arizona licensed seven new captives

The Arizona Captive Insurance Division approved seven new captives in 2015—five pure captives and two pure reinsurance captives.



Although Arizona licensed seven captives, 11 captives terminated their contracts, meaning the state suffered a net loss of four and ended up 4 percent down on 2014's activities.

Arizona currently licenses 110 captive insurance entities.

The captives licensed in 2015 came from a range of industries, including the financial, scientific and transportation sectors.

Captives that are active in Arizona include Apple Insurance Company, Hyundai Capital Insurance Company and Heinz-Noble.

### Utility reinsurer has financial strength

Fitch has affirmed the "BBB+" insurer financial strength rating of Maxseguros EPM Re.

The rating is in line with the rating of Maxseguros's parent, Empresas Publicas de Medellin (EPM), a state-owned Brazilian utility.

Maxseguros, based in Bermuda, is a core captive reinsurance company of EPM.

Maxseguros controls EPM's insurance programmes and is part of its strategic plan to seek optimum retentions and to have better control of its risk and exposures. In addition, Maxseguros provides technical optimisation in the insurance programme.

The captive's capital position has also strengthened over the last five years.

Its total capital was \$40.6 million at the end of September 2015, compared to \$3.06 million at the end of 2010.

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## Aon launches US STS scenario model

Aon Benfield's Impact Forecasting has launched its US severe thunderstorm (STS) scenario model to help insurers more accurately estimate annual losses based on historical data.

Severe thunderstorms can produce damaging winds in excess of 57 mph, hail of one inch in diameter or greater, and occasionally tornadoes.

According to Aon, the costliest US thunderstorm outbreak on record occurred in late April 2011 across the Lower Mississippi Valley, and cost insurers \$7.7 billion.

Aon claims that over the last 10 years, severe thunderstorms have overtaken tropical cyclones as the costliest peril for US insurers on an average annual basis.

The new model, STS RePlay, incorporates the last 12 years of historical severe thunderstorm data from the Storm Prediction Center and replays it to create nearly 7.5 million scenarios that are used to calculate average annual losses.

Stephen Hofmann, executive managing director at Aon Benfield, said: "The roll out

of Impact Forecasting's new STS model now means that insurers and reinsurers can effectively manage their risk and use the model's transparency to explain the details of their loss numbers and create their own view of risk from this peril."

## Sorford Surety Insurance 'under review'

A.M. Best has placed IBT Group's captive, Sorford Surety Insurance Company, under review with negative implications.

The rating agency has also given Sorford Surety, which is domiciled in Bermuda, the financial strength rating of "B (Fair)" and the issuer credit rating of "bb".

Sorford Surety is a wholly owned subsidiary of IBT Group, which is a subsidiary of Eurofinsa.

IBT and Eurofinsa are members of a multinational group of companies that specialise in the development, design, construction, equipment and finance of public infrastructure projects.

The 'under review' status reflects A.M. Best's concern with the implementation and execution risk of the captive's business plan, and uncertainty to the final outcome of its ratings.

According to A.M. Best, the ratings will remain under review for 30 days while it attempts to collate the necessary information required to assess the company's rating fundamentals.

## 'Excellent' ratings for BNY Mellon captives

A.M. Best has affirmed the financial strength and issuer credit ratings of BNY Trade Insurance and The Hamilton Insurance Corporation.

The "A (Excellent)" and "a+" ratings of the BNY Mellon captives reflect both companies' strong capitalisation, consistent operating performance, solid liquidity and conservative operating strategy.

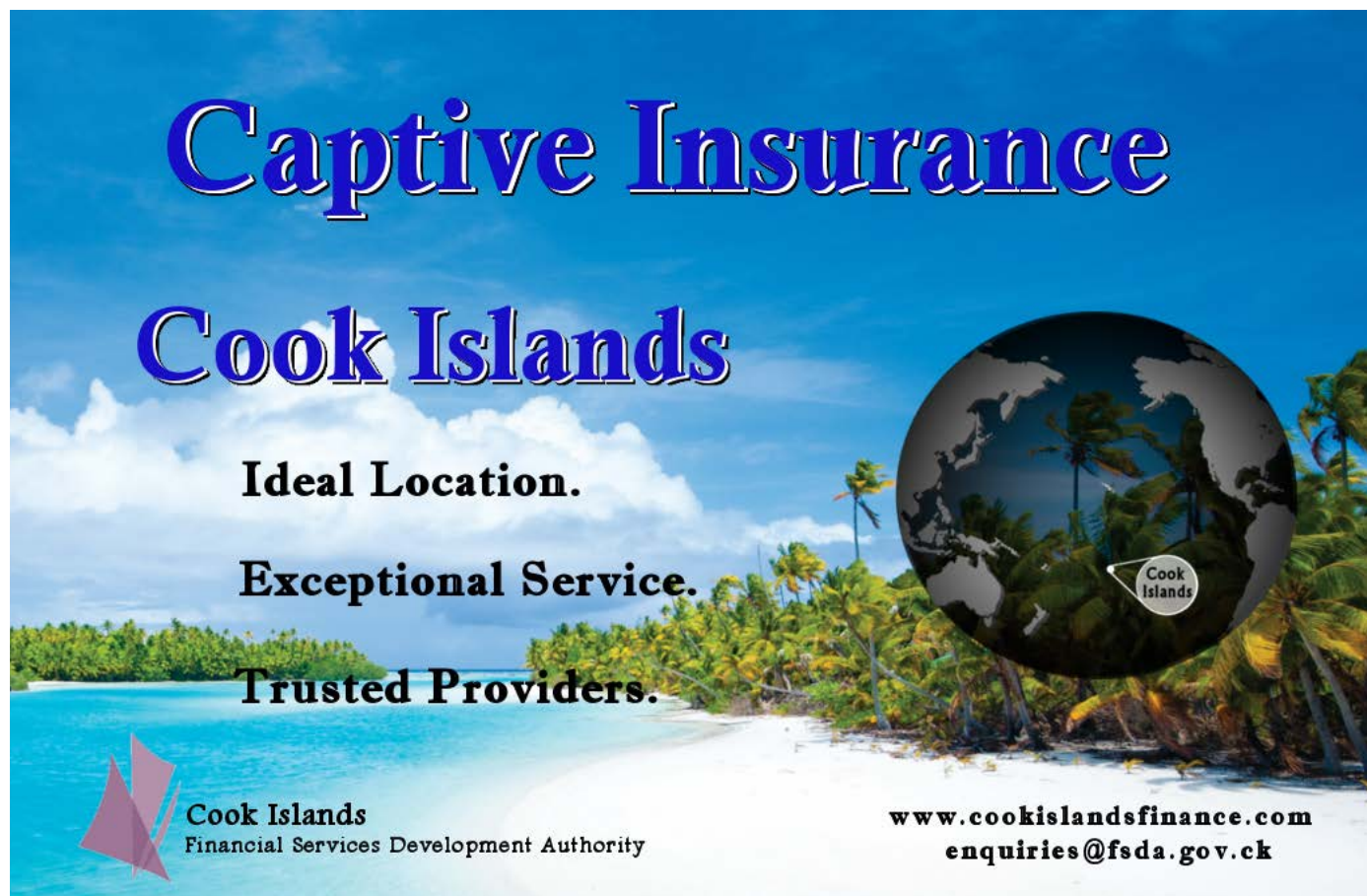
Partially offsetting these positive rating factors are the companies' limited market scope, business profile and product mix, according to A.M. Best.

In addition, A.M. Best notes that the ratings recognise BNY Trade and Hamilton's robust enterprise risk management (ERM) frameworks, as they follow the ERM practices of their parent, BNY Mellon.

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## Europe - Insurance Opportunities for US firms

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Finance Malta with support of PKF Malta are organizing a conference which will focus on what Malta can offer to US Captives seeking to tap into their European risks. The benefits of setting up in Malta as the domicile of choice.

Stakeholders from the Insurance market including MFSA and MIMA have been invited to participate, whilst a line-up of confirmed prominent speakers specialized in the US market, include individuals with years of experience in addressing the needs of US Captives with European exposures, with all its connotations of tax, domicile choice, solvency II, PCC structures etc.



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## Licensing me softly

The prolonged soft market aside, captives aren't doing too badly right now

The captive insurance industry has been at the behest of a soft market for a considerable amount of time. Peter Child, director at Artex Risk, says: "The current soft market is unprecedented."

"[It's been a] perfect storm of a comparatively low level of catastrophic losses and the desire of new capital to find investments that have provided a decent return over the last few years and present risks that are uncorrelated with more traditional asset classes."

"I have no doubt that at some point things will change, as either the value of catastrophic losses spikes or alternative investments become more attractive, but, as always, it is extremely difficult to pinpoint when this might happen."

Edward Koral, a specialist leader at Deloitte, also believes that a few catastrophic losses could change the situation, but he suggests that the market has also seen non-traditional capital, such as catastrophe bonds, play an increasingly important role. He explains: "Persistently low returns on investments could drive higher premium pricing, but we've had low returns for years now, and we still have that soft market."

Leslie Boughner, chairman of Advantage's business insurance division, agrees: "While there have been limited catastrophes that would be the catalyst to change the market, it is only a matter of time."

Is the prolonged soft market having a negative effect on captive insurance? Shelby Weldon, director of licensing and authorisations at the Bermuda Monetary Authority (BMA), suggests it is having a more significant and negative impact on the commercial insurance market than the captive market. "We continue to see interest in the captive solution, despite a slower growth rate, particularly from emerging markets in recent years," he says.

Koral argues: "We just completed a very solid year in captive formations, in the midst of a soft insurance market."

He adds that the soft insurance market occurred alongside important developments in the tax treatment of captives and new corporate structures becoming available, which draw in smaller sized parent companies.

Boughner believes that soft markets are a routine variable affecting the insurance industry. He says: "The current cycle is no different than previous cycles and successful insurance entities adjust accordingly. Unsuccessful insurance entities react and find themselves unable to adjust when market conditions harden."

According to Koral, it has also encouraged organisations that previously might not have considered forming captives to look seriously at them to solve some very specific, and boutique-like, insurance and risk management problems.

There are many reasons companies choose to utilise a captive insurer to manage and mitigate risks. Weldon says: "In our experience cheaper rates are becoming less of a significant criterion when considering forming a new captive or continuing with an existing one. Companies are taking a long-term view of their risk management solutions and captives remain a viable strategy in this regard."

"The operational advantages of captives for maintaining insurance capacity and rate stability remain highly attractive to risk managers who are examining their enterprise risk management (ERM) programmes, and assessing what exposures should be insured or self-insured."

He explains that in Bermuda captives have been formed to cover a wide range of risks. He notes: "These have included extreme weather events in Africa, workers' compensation, property and product liability, as well as oil and natural gas drilling in Canada and auto liability insurance in Peru."

### At full steam in 2015

Bermuda "continued to attract new captive registrations despite fierce competition from other domiciles and [the] continuing soft commercial market" in 2015, says Weldon.

In 2015, Bermuda registered 64 new insurers and reinsurers, only one fewer than 2014, with captive registrations defying the soft market conditions to achieve growth.

Child claims that Guernsey's predictions for 2015's captive results were "pretty much spot on". He reveals that Guernsey saw the total number of licensed entities increase from 797 to 804.

Although the number increased slightly, he notes: "There was a net nil change in the number of standalone captive entities, with 13 new formations and 13 surrenders. The growth came from new protected cell company (PCC) and incorporated cell company (ICC) cells."

Child adds: "We all know that the environment is not wholly conducive for new captive formations, so to be able to maintain the number of captives and grow the number of cells is encouraging for the island."

Boughner reveals that while Cayman Island captive formation figures were not as robust as some US domiciles, Cayman continues to experience growth in US healthcare.

He adds: "You have to consider that Cayman is not a centre for US micro captives, which will distort the numbers, but continues to be a captive leader when measured by premium and assets."

Cayman licensed 22 new captives in 2015, mirroring the number of captive formations in 2014. At 2015's Cayman Captive Forum, Patrick Bodden, the Cayman Islands Monetary Authority deputy managing director, revealed that 189 new captives have been licensed between 2010 and 2015.

With 2015's captive formation figures as expected for most, Koral believes "it is a sign of returning marketplace confidence". Vermont, for example, experienced strong growth in 2015, licensing 16 companies throughout the year.

Koral says: "A few years back you couldn't get companies to even look at new captive formations, even when initial cost benefit analysis showed a strong green light."

"But that's changed. Practitioners continue to innovate and think up new uses for captives, and there are fewer and fewer barriers to formation."

With captive insurance still popular, will 2016 be another positive year despite the prolonged soft insurance market?

Boughner responds with his own question: "Why would a company not have a captive?"

"A captive provides direct access to the reinsurance market. In hard cycles they can access capacity, which is not available as direct capacity. It can also retain risk within the captive at very attractive rates."

"In soft cycles the captive provides a vehicle to arbitrage the market at attractive costs. Neither option is available to companies who do not have a captive."

Koral believes nothing has happened over the past few years to make captives less attractive. He predicts that 2016 will be a strong year, and believes 2017 could be even stronger. He says: "The changes made to the small insurance companies provision in the US Tax Code are designed to root out potential abuses, but they also create opportunities for small to mid-sized companies that may have been waiting on the sidelines."

According to Weldon, it is the BMA's job to provide a stable supervisory environment that contributes to the interest in the captive solution.

He says: "If we continue to provide that kind of oxygen to the marketplace at the level of quality demanded of us, then there is every chance that this industry will continue to thrive."

Child, on the other hand, is against any predictions about the future, stating they are "fraught with danger".

But he does believe that "if the insurance management industry continues to diversify its activities and provides insurance-based solutions to a wider audience, there is potential for a better 2016, even if the environment is as challenging as it was in 2015". **CIT**

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# The aim of the claim

Crawford & Company's Benedict Burke believes that captives should consider the customer journey when settling claims made against them

## What is the key to successful claims management for worldwide captive programmes?

The key to successful claims management for worldwide captive programmes is in the collection of accurate data, pursuit of recoveries and ultimately the protection of businesses and brands.

With every passing year, the actions of captive insurers behind global brands become increasingly influential.

Their acquisition of claims data over time means those subtle changes to an organisation's risk profile can be made, helping to reduce exposures and allowing the business to move with the times.

This can be seen in the removal of hazardous revolving doors at hotels or sharp edges at the dining tables of chain restaurants.

## Do you manage claim needs in multiple locations around the world?

As a global third-party administrator (TPA), Crawford's TPA business, Broadspire, supports businesses around the world with its claims handling.

By nature, businesses want to keep administration light and this means we can pick up the slack for them when claims occur. The most obvious example is in how first notification of loss is handled.

We act as the local insurance manager, but operate a lean system to ensure data collection is the immediate priority after the safety of employees, customers and property.

Collecting information as quickly as possible after an incident has occurred means that data can be aggregated and leveraged to make strategic decisions, helping risk managers to reach that elusive 'single version of the truth'.

Of course, no system is perfect, but without a uniform and systemised approach the process will be flawed and claims defensibility rendered much weaker.

## What types of claims do you work with?

Broadspire TPA manages the entire range of claims from personal injury, property damage, business interruption, right through to reinsurance.

## How do the claims needs of captives differ from traditional insurers?

From the most obvious standpoint, they have only one 'customer' and as such the captive is an extension of the business itself. Captives should be considering the customer journey when they settle claims made against them, particularly when a TPA is acting on their behalf.

Does the corporate provide authorisation for the TPA to use assets that are unique to that brand as a means of compensating people in addition to a financial settlement? If the claimant was a guest or a paying customer, they clearly wanted to associate with the brand in some form before their loss, so equipping your claims teams with benefits, goods or services can really enhance the journey for everyone.

## How do you work with captive insurers to reduce unnecessary claims and the associated costs?

There are many approaches that can help reduce unnecessary or attritional claims, and it very much depends on the nature of the organisation.

If the captive is responsible for insuring staff and property in a manufacturing context then we would seek to implement more stringent health and safety risk management programmes, supported by robust data collection of insured and uninsured risk at first notification of loss.

If the business had a more significant 'shop window' exposure with public liability risks, the emphasis would be on maintaining a safe environment for customers and so on.

Essentially, we always advise a robust stewardship programme that is aimed at constant improvement. **CIT**

“ They have only one 'customer' and as such the captive is an extension of the business itself ”

Benedict Burke, Head of global markets, Crawford & Company



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# The price is sharing

Cassatt Insurance Company's Eric Dethlefs reveals how the healthcare group captive's members work together to share best practices and risk

## Who are Cassatt's members and what do they have in common in terms of risks?

Cassatt Insurance Company's members are independent, non-profit hospitals and healthcare organisations located in Southeastern Pennsylvania. They share the risk of financial and other losses due to medical liability and malpractice claims.

## Why did they opt for the group captive model for their insurance coverage needs?

During the past few decades, obtaining access to affordable and reliable hospital excess liability and malpractice coverage in the commercial marketplace has presented significant and widespread challenges for hospitals and healthcare organisations that must insure risk.

In response to the turmoil in the traditional insurance market, in 1991 a group of independent, non-profit hospitals in Southeastern Pennsylvania formed Cassatt Insurance Company. This captive insurer, domiciled in Bermuda, provided excess professional and general liability coverage on a 'shared' basis for the group members.

Cassatt's purpose from the beginning has been, and remains, to provide an insurance platform on which its members can work together to share knowledge, best practices and risk, and in doing so, improve patient safety and outcomes throughout their hospitals. As a result, they are able to reduce the incidence of claims and lower their liability costs.

## What benefits does the group captive model offer in terms of risk sharing and funding?

Because a group captive is wholly owned and controlled by its insureds sharing risk, there is an inherent, strong commitment among its members to ensure safer outcomes at their hospitals. Cassatt's member-owners are relentlessly focused on improving safety and outcomes for their patients. As a natural result of creating safer hospitals, their risk and liability costs are significantly reduced.

Another benefit of Cassatt's model is that it incorporates a sponsored captive or, put in other terms, a segregated cell captive.

In October of 2013, Cassatt became Vermont's thousandth licensed captive.

In doing so, the captive is designed to provide insurance coverage flexibility for members as they merge and form affiliations with other hospital systems in the future, address the Affordable Care Act and other challenges.

## Do the hospitals share best practices and knowledge to keep the costs of claims down? If so, can you provide some examples?

Yes. From its founding, Cassatt was defined by a culture of sharing—independent members worked collegially to share best practices, coordinate risk management efforts, focus intensely on claims management, and improve the quality of healthcare in their facilities.

One of the other unique aspects of Cassatt is that the CEOs and other senior executives of its member hospitals, from both the clinical and business sides of their organisations, are also represented on the Cassatt board of directors.

This collective and cooperative approach among our membership is not present in traditional commercial insurance programmes, and is very unusual among other captive groups.

## How are Cassatt and its members innovating to ensure patient safety?

In 2012, the Cassatt Patient Safety Organization (PSO) was approved by the US Department of Health and Human Services's Agency for Healthcare Research and Quality Control (AHRQ).

Its purpose is to create a collaborative and confidential environment of learning and knowledge exchange among our members, substantially enhancing their efforts to improve patient safety and quality of healthcare throughout their hospitals.

The power of the PSO comes from the sharing of experience and information. By collecting and analysing data and sharing information and experience from all of our members, the PSO is able to identify problems and trends that an individual hospital alone might not be able to detect.

Most captives do not do what Cassatt does in terms of creating and facilitating this kind of shared learning environment. **CIT**

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From its founding, Cassatt Insurance Company was defined by a culture of sharing

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Eric Dethlefs, President and CEO, Cassatt





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# Boss of the stop-loss

A greater risk distribution is achieved by adding medical stop-loss to captives that insure other lines of coverage, explains Lance McNeel of Capstone

The Patient Protection and Affordable Care Act (ACA) has had the tendency to push a greater number of middle-market companies into self-funding their healthcare programmes and buying medical stop-loss insurance to protect them from catastrophic claims experience. The concept is simple. Rather than using a fully insured plan, the employer sponsors a self-funded health benefit plan and includes medical stop-loss coverage through the commercial insurance market, a captive insurance company, or a combination of the two. Reasons for taking this approach include: reducing overall costs associated with state premium taxes and ACA requirements, providing greater control over the plan design, and taking advantage of a younger and healthier workforce to avoid the adverse selection encountered by the insurance exchanges.

A primary advantage to using a medical stop-loss programme is that the regulatory burden is greatly reduced because these plans are not considered an employee benefit programme under the Employee Retirement Income Security Act and so prior approval is not needed from the Department of Labor. This is primarily due to the fact that the policy covers the employer for catastrophic loss experience associated with a self-funded health benefit plan. For this reason, it also cannot be considered a third-party risk.

There are additional benefits when a captive is included in the plan, such as greater tax efficiency, and the ability to minimise the

effects of exclusions in the commercial insurer (often referred to as a reinsurer) medical stop-loss coverage, the ability to smooth out claims volatility from year to year and the ability to customise the terms and attachment points at the division level.

Also, greater risk distribution is achieved by adding medical stop-loss to captives that insure other lines of coverage. The use of a captive to insure all or part of a medical stop-loss programme provides significant benefits for the right companies.

## The structure of a medical stop-loss programme

The stop-loss coverage can be either specific or aggregate, or a combination of these. Specific stop-loss covers claims in excess of an amount for any covered individual.

Aggregate stop-loss covers the risk that the total of all claims within the policy period exceeds a stop-loss threshold. These two forms of medical stop loss are often purchased together.

The structure of each medical stop-loss programme can take many forms, including:

- The employer purchases the medical stop-loss coverage from a commercial insurer and self-insures all losses under the stop-loss attachment point.

- The employer purchases the medical stop-loss coverage from a captive insurer and self-insures all losses under the stop loss attachment point. The captive may be owned by or affiliated with the employer as a single parent captive, exist as part of a captive cell company (generally for smaller employers), or be a group captive.
- The employer purchases the medical stop-loss coverage from a commercial insurer that cedes a layer to the captive insurer. The employer then self-insures all losses under the stop loss attachment point.

There are countless combinations of how the layers can be pieced together based on the individual goals of the employer. The factors to be considered in the planning process consist of having a coordinated team of experts, including a benefits consultant, programme administrator, claims manager, medical stop-loss provider, captive manager, actuaries and experienced legal counsel.

### Considerations in forming the captive

Employers that want to use a captive to participate in a medical stop-loss programme will also need to analyse the feasibility of forming the captive for that purpose. There are legal, tax and regulatory considerations in addition to the technical risk management issues. The legal structure, ownership and corporate governance need to be seriously addressed.

Also, multiple layers of tax planning should be addressed, including federal and state income taxes of the employer associated with the deductibility of premium payments, state premium taxes of the captive, and issues involving the definition of insurance from the perspective of the Internal Revenue Service.

The relative merits of the regulatory environments of the many captive domiciles should also be assessed in relation to the goals of the employer.

These and other considerations are to be addressed by competent experts as part of the feasibility study. In the case of medical stop-loss, an actuarial study should be the first step to make certain that the employee census and the resulting loss experience can support a medical stop-loss programme and to identify alternative costs associated with different attachment points in light of the employer's level of risk aversion.

Once the actuarial analysis is complete, pro forma financial statements covering the next five years should be generated for both the expected scenario and an adverse scenario to assess the

surplus requirements and rate adequacy. These pro forma financial statements will then be included in a detailed business plan to guide the formation and implementation of the captive.

Once the feasibility analysis is complete and the parties agree that the use of a captive insurance company to participate in a medical stop-loss programme is feasible and the preferred option, the captive will be formed in the appropriate domicile, the sponsored plan should be created and the reinsurer identified. The captive will be incorporated and licensed to issue the medical stop-loss policy and any other policies that fit into the overall programme. Finally, the other service providers will be identified and brought into the overall programme.

Self-funded health benefits plans are not new, and neither is the use of medical stop-loss coverage to protect against catastrophic losses or high aggregate losses.

These plans have been used by larger employers for many years. However, the ACA changed the rules for these programmes by making fully insured programmes significantly more costly. This in turn has pushed the point where medical stop-loss programmes make sense to smaller middle-market employers.

The reduced cost of these plans compared to fully insured plans, along with other significant benefits—such as greater control over plan design and the ability to avoid the adverse selection that is causing chaos in the commercial market and the exchanges—creates incentives to form captives and utilise stop-loss policies that did not exist before the passage of the ACA.

Since many of these middle-market employers currently use captive planning to manage other operational risks, it is a natural tendency to include medical stop-loss coverage in the existing captive, or to form a separate captive for that purpose.

While some states are hostile to the trend and are exploring ways to increase minimum attachment points in order to squeeze smaller employers out of the market, other states are embracing the concept.

The formation of a medical stop-loss captive is not a simple project, so great care should be taken to secure knowledgeable strategic partners that will lead you away from the many pitfalls that can arise. However, with the right team, proper planning and a supportive corporate culture, medical stop-loss programmes that include a captive insurance company can provide powerful benefits. **CIT**

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The formation of a medical stop-loss captive is not a simple project, so great care should be taken to secure knowledgeable strategic partners

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**Lance McNeel**, Vice president of business development,  
Capstone Associated Services





## North Carolina is coming

The state was one of the standout US domiciles for new formations during 2015. Debbie Walker of the North Carolina Department of Insurance reveals why

### How has North Carolina's captive programme grown since its inception in 2013?

The programme has grown in several ways. During the last two full years, the number of captive insurers licensed in North Carolina has increased to 96, and the number of cells or series has increased to 240.

The number of captive managers that are active in the North Carolina captive insurance company programme continues to grow. Currently, there are 23 captive managers actively managing North Carolina's licensed captive insurers.

North Carolina's captive service provider base also continues to grow. Today, there are more service providers, such as auditors, attorneys, investment advisors, captive managers and others, that have a physical presence in this state.

Additionally, there are many providers from outside of North Carolina that are active in our captive industry.

Due to the growth of the captive industry, North Carolina is benefiting from job growth and the receipt of increased premium tax revenue, service provider revenues and hospitality revenues, resulting in a favourable economic impact on the state.

Finally, the North Carolina Department of Insurance, the North Carolina Captive Insurance Association and the legislative leadership of the state are continually addressing national issues that have an impact on the captive insurance company industry.

### What factors do you believe have contributed to the success of the North Carolina's captive programme?

The North Carolina Captive Insurance Act provides the state's insurance commissioner with discretion to appropriately regulate captive insurance companies. Our legislation is structured so that a one-size-fits-all regulatory framework is not imposed on captive insurance companies licensed in North Carolina.

The participation by the department's senior management in the captive insurance programme is unique from what is seen in other captive insurance company domiciles. Our senior management team is accessible and available for conference calls and meetings to discuss our captive programme. Additionally, the captive regulatory team is professional, helpful and responsive to the captive insurance company industry.

The North Carolina Captive Insurance Act and the Department of Insurance's regulatory approach allow for low costs for captive insurers and the programme has benefited from the support and contributions of the North Carolina Captive Insurance Association, captive insurer owners, captive managers, and other service providers.

### What do you think makes North Carolina stand out from other competitive domiciles?

There are a number of benefits to forming a captive insurance company in North Carolina. First, North Carolina's law provides the state's insurance commissioner with discretion to regulate each captive insurance company as deemed appropriate. Not being tied to a one-

size-fits-all approach, we subscribe to financial requirements that are tailored to the specific risk profile of each captive insurance company.

The North Carolina Department of Insurance's regulatory approach provides for a low cost of captive insurance company operations in North Carolina. For instance, the department does not charge any fees whatsoever. Also, the department does not contract with outside consultants. It uses in-house analysts, auditors and actuaries to conduct all application reviews, financial filing reviews, and audits, so that expenses are not passed on to the captive insurers, as is done in some other jurisdictions. These are just some of the factors contributing to the lower costs of operation.

In addition, the Department of Insurance takes a smart, sensible, pro-business approach in its regulation of captive insurers. By this we mean our regulatory approach is effective and prudent but not burdensome for North Carolina captive insurance companies.

Our intent is to focus more of our resources on those captive insurers that require additional regulatory scrutiny and allow the well-managed, successful captives to conduct their business with less regulatory involvement.

The department is dedicated to providing outstanding customer service to the captive insurance company industry. Our senior management and our captive regulatory team are accessible and available for telephone calls, meetings and educational events. We are reaching out to businesses and their trusted advisors to educate them about the use of captive insurance for the management of their risks and the North Carolina captive insurance company programme.

### Was 2015 a successful year? How many captives did you license?

Yes, the North Carolina Department of Insurance is very excited about the success of the captive insurance programme in 2015. In total, 42 captive insurance companies were licensed during the year (with two more approved for licensing in 2016), bringing the total number of approved captives in the state to 96. Additionally, the department approved 120 business plans, bringing the total number of approved cell business plans to 240. In total, 336 risk-bearing entities are currently approved to operate in North Carolina.

### What type of captives did you license? And from which sectors?

During 2015, the North Carolina Department of Insurance licensed 32 pure captives, two protected cell captives, and eight special purpose captives. In addition, two risk retention groups were licensed for 2016.

With the addition of the new captive insurers described above, our totals for each type are 71 pure captives, 13 protected cell captives, 10 special purpose captives and two risk retention groups.

These captive insurers provide insurance to many types of industries, including: energy; home health care; automotive; transportation and logistics; physician and dental practices; equipment leasing; real estate investment companies; information technology; heating, ventilation and air conditioning, electrical, and plumbing; construction; steel distributors; warehousing and distribution centres; and manufacturing companies.

### Do you expect to see growth continue during 2016?

We do anticipate another year of strong growth in North Carolina during 2016. To encourage this, we plan to: continue our

participation in national, state and local captive insurance company educational events; meet with captive managers, business owners and other trusted advisors to tell them about the North Carolina captive insurance company programme; and provide outstanding service to the industry.

### Are there any regulation updates due in 2016?

The North Carolina Department of Insurance plans to submit a legislative amendment proposal for the 2016 legislative session as we have done during 2014 and 2015.

We treat the act as a living document, continuously reviewing it and determining if amendments are necessary in order for the act to remain relevant to, and competitive within, the captive insurance company industry. **CIT**



North Carolina's law provides the state's insurance commissioner with discretion to regulate each captive insurance company as deemed appropriate



**Debbie Walker**  
Deputy commissioner of the captive insurance  
companies division  
North Carolina Department of Insurance





# Cleaning

out my captive (one more time)

Changes to the 831(b) tax election, set for 2017, could go some way towards small captives shedding their 'dirty dozen' status. Brady Young of Strategic Risk Solutions tells Becky Butcher how

## Why has there been such an increase in captives making the Section 831(b) tax code election over the last five years?

As the US economy has recovered, business owners have had the financial ability to think more long term and have elected to set up captives to address many of the risks and threats they face in their businesses where the traditional insurance market has been unable to provide coverages.

I also think the growth has been due to aggressive sales and promotion by several captive managers that specialise in the space, resulting in brokers and clients becoming more familiar with the concept of a captive and the long-term benefits that captives can provide. Medium-sized companies have a better concept of enterprise risk.

Many are now thinking beyond the basic lines of insurable risk and are being introduced to the concept that there might be ways to finance risks more efficiently that were just accepted as being part of operations, and handled on a pay-as-you-go basis.

## What about the proposed changes to the 831(b) tax election?

The changes were buried in the tax extension bill that was passed at the end of 2015 and will go into effect for the 2017 tax year.

It's somewhat confusing to everyone how to interpret certain aspects of the new qualifications, but the main changes and highlights include: (i) the premium cap to be able to qualify as a small insurer has been lifted from \$1.2 million to \$2.2 million and will be adjusted for inflation going forward; and (ii) the ownership of the captive must largely mirror the ownership of the insured(s) (from an estate perspective), or no more than 20 percent can come from one policyholder.

## Do you think there will be a positive impact from these changes? And do you think there are issues to be considered?

I believe there are many positives with the changes, starting with the higher premium allowance, which will help many existing captive owners that have the ability to fund higher premiums in order to have their captives provide more capacity to address the major risks they face in their businesses.

In addition, it will attract new captive owners that may have looked at having a captive for some low-frequency, high-severity risks but felt the current premium limit was just too small for them to build up meaningful capacity for a major loss exposure.

I also think the changes will result in a bit of a clean-up of some captives that were set up for the wrong reasons, and hopefully will squeeze out some of the overly aggressive captive promoters who were positioning captives more as estate planning vehicles than as risk management and insurance tools.

In the meantime, many captive owners are going to make changes in their ownership structures and reconsider their business plans to provide more limits of protection for existing policies underwritten, as well as additional coverages.

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A proper analysis should be made to determine the best course of action, as once made, the election is irrevocable

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**Brady Young**, President and CEO,  
Strategic Risk Solutions



## Do you think the premium limit increase will have an effect?

Yes, for companies that have additional risks or needs and have the ability to pay the additional premium. We also expect some medium-sized captives writing traditional lines of insurance, such as workers' compensation and liability, to opt for the 831(b) election instead of the 831(a) large insurer election.

The higher premium limit, for those that can justify it, will also reduce the relative cost (as a percent of annual premiums) to set up and operate a captive and make the economics more compelling for many captive owners.

## After the IRS identified captives as one of its 'dirty dozen' targets last year, what concerns does the agency still have?

I cannot speak for the Internal Revenue Service (IRS), but from the amount of audit activity and litigation taking place, it has clearly focused on certain structures and management firms that it perceives as having been overly aggressive in the use of small captives.

The main issues appear to be captives writing questionable coverages (does the client really have that exposure?) or charging 'excessive' premiums that have no actuarial or market basis. I think another concern has been with captives that appear to be driven by estate tax goals, as opposed to solid risk management and business objectives. Finally, captives investing in questionable asset classes, including life insurance, are not viewed favourably.

## Are there any negatives to making, or qualifying for, the 831(b) election that prospective captive owners should be aware of?

There can be. In the event the captive suffers underwriting losses, such losses are not deductible as they would be for a captive taxed as a traditional insurer, under 831(a). Furthermore, if the captive experiences a net operating loss due to adverse claims experience, such net operating loss cannot be carried back to offset prior taxable income or forward to be used in future years.

Obviously, the premium limit puts a cap or limit on how much premium can be paid, which may preclude clients covering all the risks they want or need to address. The 831(b) election is not for all programmes. A proper analysis should be made to determine the best course of action, as once made, the election is irrevocable. Finally, captives filing on this basis are likely to be subject to more scrutiny compared to large captives. **CIT**

# Desert blooms

The lone star state is striving to be a nurturing environment for captives, say TxCIA president Josh Magden and conference committee chair Julie Patel

## How many attendees are you expecting for 2016's Annual TxCIA Conference? What can delegates expect?

**Josh Magden:** We have had over 100 attendees to each of the first two conferences, and given that the conference is to be held in Houston this year, we expect north of 150 attendees, including many local businesses and new captive owners.

Despite the downturn in oil prices, the energy industry will likely have strong representation.

These are the type of markets where seasoned hands will start to look for entrepreneurial solutions to hold costs in check, develop alternative revenue streams and build corporate infrastructure that will help them weather episodic price volatility.

Additionally, general industry awareness of Texas's expanded statute, and the efforts by the Texas Captive Insurance Association (TxCIA) board and membership, is building interest.

That has led many Texas business owners and corporate risk managers to explore whether it benefits their organisation to start a new captive or re-domesticate an existing captive. We expect to have great participation as conference attendees have an interactive dialogue with speakers and other attendees.

## What hot topics will be discussed at this year's conference?

**Julie Patel:** The agenda this year includes sessions such as: TxCIA Captive Legislative Initiatives—2015 Developments and Beyond; Trends in Captive Utilisation; The 'Taxing' Challenges Today in Having a Captive; Insuring Employee Benefits in Your Captive: The Real Benefit to Captive Owners; The Dos and Don'ts for the Texas Captive Application Process; Life of a Captive in Operation; When Do You Need a Checkup for Your Captive?; and a Client and Prospect Roundtable.

The Captive 101 session last year was at full capacity and this year we will once again kick off the conference with this popular event. Texas is still a new enough domicile that many prospective and existing captive owners and service providers appreciate the chance to gain insight into the workings of a captive and their opportunities to domicile in Texas. With regards to key topics for captive owners, the tax panel and the employee benefits session are timely.

Additionally, we will have a client and prospect roundtable after the conference has officially concluded. This session is designed to allow current Texas captive owners and prospects to have discussions privately among themselves.

We're quite excited this year to have the opportunity to invite undergraduate and graduate students from several schools around the state to attend the pre-conference '101' session. They can meet with TxCIA members and conference attendees, and better understand the alternative risk industry, as well as gain insight into professional options within corporate risk management and the captive sector.

We're proud to say that one of our own board members is sponsoring scholarships for student attendees to the conference. We want to begin to build a long-term relationship and a sense of common purpose between the business, academic and governmental participants in the captive industry here in Texas.

## What sessions are you most looking forward to?

**Magden:** We are looking forward to all the sessions, but one that may be of interest to many of the attendees is The 'Taxing' Challenges Today in Having a Captive session. The speakers for this session, Tom Jones, Chaz Lavelle, and Dan Kusaila, will provide insight on the latest developments regarding the taxation of captive insurance companies.

This panel of tax specialists will also comment on the latest developments affecting captive insurance companies and the recent changes in the 2015 Tax Extender bill, which affects some 831(b) captives.

The session on employee benefits will be presented by Gary Osborne, who is president of USA Risk Group. The Affordable Care Act is driving expansive shifts across the scope of healthcare, health insurance and employee benefits, and this will be a wonderful opportunity to hear from an industry veteran on precisely where the opportunities and potential challenges lie for captive owners.

We are also very excited about the keynote speaker, Bob Hamman, a TxCIA member, the owner of SCA Promotions, and a 13-time international bridge champion. His firm is unique in running promotional prize contests and insuring sponsors, in items like hole-in-one jackpots, half-court basketball shots or \$10 million in free Taco Bell tacos. He has some fascinating experience from both spheres of his career.

## What will TxCIA be working on in 2016 in terms of captives?

**Patel:** The legislative agenda is still under development. In Texas, the legislature meets every other year, however, the association and captive members are working through some of the rulemaking process from the expansion of the statute that occurred in 2015's legislative session.

## Does 2016 have anything else in store for TxCIA?

**Magden:** It certainly does, we just don't know what it all is, as yet. We have grown quite a lot as an organisation and have a very strong board of directors with a diverse set of experiences and perspectives. The legislative objectives that develop through the timeframe of our conference will guide much of the association's activity in the latter half of the year, beyond our general outreach and educational efforts.

TxCIA wants to grow membership and, within the parameters of our Texas statute, do everything we can to help to build a domicile where company owners are best able to use their captive to protect and grow their business. **CIT**



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## Running away with it

The captive market is seeing more and more run-offs. SOBC Corp will be there to get them on the right track, say Tom Hodson and Stephanie Mocatta

**How commonly are captive run-offs occurring in the current financial climate? Today, is it more of a business decision or a financial one?**

**Tom Hodson:** Captives, by their nature, are organised as a risk management solution for a single parent or small group of parents. The captive's continuing ability to cover loss is paramount to the parent's, or parents', ability to successfully manage risk. As a result, insolvencies in the captive market are rare.

Most captives in run-off are the result of a business decision by the owner. The business reasons to close a captive vary, but can include a change in strategic direction by the company, a change in market conditions, or a change in regulatory climate. For example, in 2008, as the US stock markets declined, captive owners found it increasingly difficult for investment income to support their underwriting. In some cases, competing needs for capital meant the captive could no longer be supported, and was placed in run-off.

In addition to captives in run-off, one of the areas that SOBC Corp is focused on is buying 'old year' liabilities from captive owners. In many fronted programmes, owners are required to 'stack' collateral, which, depending on the tail of the business and the terms demanded by their fronting carrier, could get very expensive. SOBC Corp will look to relieve captive owners of their old year liabilities, allowing the release of collateral to be applied to future years.

**Where companies are acquiring additional captives through mergers or acquisition, are you seeing a higher demand for captive run-offs?**

**Stephanie Mocatta:** One of the most exciting areas of potential growth for SOBC Corp is in the acquisition and run-off of 'redundant' captives. As captive insurance is popularised and more and more companies manage risk through captive programmes, there is a growing market in companies owning two, three or more captives acquired through mergers and acquisitions.

For many of those companies, insurance is not their primary business, and SOBC Corp can be a helpful resource, assisting

them in effectively and efficiently dealing with any legacy business acquired through mergers and acquisitions.

**How would you best describe the run-off acquisition service that SOBC Corp provides?**

**Hodson:** SOBC Corp provides a much-needed filler for a gap in the run-off acquisition market—the acquisition of smaller or significantly distressed insurance entities.

Many of the major players will only look at companies of a significant size, or those where there is a potential for a quick return—in terms of run-off. Our capital structure is such that the management team owns 50 percent of the company and our capital is mainly from high net worth individuals with a very long-term horizon—the majority have invested through pension funds.

This means we are able, with our committed management team, to take a long view on insurance run-offs and to provide finality for clients with difficult, litigious or complex books of business.

We also pride ourselves in acquiring companies outright—we do not ask for any warranties or indemnities on the insurance liabilities.

**SOBC Corp recently acquired Insuratex in Bermuda. What other markets have you entered, and why?**

**Mocatta:** SOBC Corp is primarily focused on the US, Bermuda and the Caribbean. The US market is a significant size, around 75 percent of the world's insurance premiums, with a very large percentage of smaller companies that fit within our target area.

There are around 2,750 property and casualty companies in the US and an estimated additional 6,500 captives and risk retention groups. We provide an exit solution for those smaller companies where finality is the ultimate goal.

The Bermuda market also offers us good opportunities, particularly in the captive area. There are a large number of captives that have entered the Bermudian market over the years,

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We have a number of additional targets where we are doing due diligence, some of which are captives and risk retention groups

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**Tom Hodson**, General counsel, SOBC Corp



some of which are officially in run-off, others are dormant. Again the major players will look at the larger companies, but will not deal with the smaller or more troubled companies that are our target market.

The Caribbean market, certainly in some of the jurisdictions, mirrors Bermuda. Many of the islands have long been captive domiciles and have captives that either are, or perhaps should be, in run-off.

SOBC Corp is extremely pleased to have Harry Whitcher as one of our directors and shareholders.

Whitcher was a regulator in both Bermuda and the British Virgin Islands (BVI) and brings excellent knowledge of these jurisdictions and also of the cross-border regulation issues.

#### **Have you considered entering the UK and Europe?**

**Hodson:** We will always consider opportunities in the UK and Europe, however, our experience suggests it is unlikely to be a significant market for SOBC Corp. This is for a number of reasons:

- The run-off market, particularly in the UK, is very mature compared to the US and Bermuda.
- The legislation in the UK and Europe, with the options for Part VII transfers protecting the reinsurance asset and schemes of arrangement for the closure of companies, has meant that a majority of the smaller run-offs have either already been closed, or have merged into larger entities.
- The UK and European markets are oversupplied with run-off providers.

#### **In addition to Insuratex, how many other captive entities have you acquired?**

**Mocatta:** SOBC Corp is a relatively new company—we formed in mid-2014 and completed our capital raise in mid-2015—Insuratex is our first acquisition as SOBC Corp. However, SOBC does build on the experience and reputation of a prior company, SOBC Limited (which was UK domiciled).

SOBC Limited made five acquisitions—one Bermudian, two in New York, one in Pennsylvania and one in Louisiana. The Pennsylvania acquisition was actually an insurance company, but acted as a captive.

SOBC Corp does see the captive market as a significant opportunity for future run-off acquisitions.

#### **Do you have any other acquisitions in the pipeline for 2016?**

**Hodson:** We have signed sale and purchase agreements on two further entities; these are now going through the change of control process. Both are onshore in the US.

We have a number of additional targets where we are doing due diligence, some of which are captives and risk retention groups.

Our business plan is to acquire multiple small entities. We are prepared to look at some very small opportunities. As we conduct our due diligence in-house we are able to commit the time necessary to look at the smaller entities and can quickly see if a deal will be possible. **CIT**



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SOBC Corp does see the captive market as a significant opportunity for future run-off acquisitions

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**Stephanie Mocatta**, CEO, SOBC Corp



# Malta is the domicile of choice for insurance vehicles in Europe

Danielle Hermansen of PKF Malta discusses how Malta can, and is, fully utilising its potential in the insurance industry

PKF is supporting Finance Malta in its quest to promote Malta, by organising a conference on 29 March 2016 that will focus on what Malta can offer to US captives seeking to tap into their European risks. It will showcase benefits of setting up in Malta as the domicile of choice.

Finance Malta, as a private/public partnership, is geared toward promoting the sector, mindful that it faces tough competition fielded by established jurisdictions. Yet it succeeds in attracting

international companies seeking an alternative to the traditional, tried and tested European jurisdictions such as Dublin.

The conference venue is the prestigious Bar Association building located at 42 West 44th Street in New York.

One may well ask, with so much competition, what Malta can offer in this sector that sets it apart from other centres such as the Isle of Man, Channel Islands and Gibraltar, or the Caribbean stalwarts

of Bermuda, Barbados and the Cayman Islands. The answer is flexible and fair regulation, a competitive fiscal regime, more than 70 double tax agreements and all of the financial services support available at a high professional level.

It is common knowledge that an insurance vehicle domiciled in an EU member state can provide cover for risks across the entire territory, subject to local regulatory requirements, and thanks to this facility, most captives take advantage of the European economic area (EEA) freedom of passporting to write insurance directly without the need of a frontier.

Malta can be said to have a firm advantage for insurance companies continuing and/or seeking to establish themselves in Europe.

With its respectable number of 62 insurance companies, nine affiliated, 12 protected cell companies (PCCs), with 27 cells, and eight insurers of domestic origin, Malta is pushing ahead to attract quality not quantity, but of course the numbers are important and no effort is to be spared to expand the internal market.

It goes without saying that a number of jurisdictions are active in pursuing captive owners and reinsurance companies, encouraging them to redomicile, so one may ask in the context of Malta, why are the numbers so modest and what can be done to overcome the challenge to attract more investors?

The answer is that as an EU member state and European Insurance and Occupational Pensions Authority member, Malta has contributed to the development of Solvency II and its expertise has grown thanks to the open dialogue with the local one-stop shop authority, the Malta Financial Services Authority.

A US captive owner wanting to set up an insurance vehicle to insure its European risks or to enter the insurance-linked securities market will find that it is mandatory to set up in Europe. They can easily set up vehicles including cells as fronting facilities in Malta in order to reduce their EEA fronting costs and reinsure back to the US.

Typically, a non-EU captive would use a licensed insurance company as the frontier to write business in the EU, with the captive then reinsuring the frontier.

However, this has its disadvantages. There are no general guidelines in EU domiciles that limit or control the amount and type of collateral that must be provided to a fronting insurance company. This collateral is trapped money that may be utilised elsewhere, so many do find the cost of setting up a cell in an EU domicile

to be more competitive, while ensuring full control of it as a risk management tool.

Captive owners therefore need to assess which solution is best to reduce the amount of collateral that becomes trapped and the ongoing costs of fronting arrangements. It is common to expect that the demand for collateral will be driven by the frontier's requirements, based on its own risk assessment and invariably will be a matter of commercial negotiation between the parties. It is also common knowledge that fronting partners assess offshore captives differently to onshore captives.

This is a potential market that Malta needs to tap into, to establish itself as one of the domiciles of choice within Europe for captive insurance and reinsurance companies.

Operating from Malta means utilising the freedom to provide services to companies that operate between EU member states, so captives can insure or provide insurance services to the vast European insurance market.

Malta can be said to have a firm advantage for insurance companies because it enjoys the enviable position in the entire EU to provide PCCs, whose cells do not suffer the additional financial costs associated with both establishing and running an insurance vehicle.

Malta is fully equipped to cater for PCC structures, since we have been the forerunners and only full EU member to have legislated these structures in the Solvency II arena in Europe. One might add that Malta will continue to introduce innovative products in the near future. The PCC concept has also been taken further to include insurance intermediaries and now securitisation cell companies.

Setting up and running these companies in Malta is reputed to cost on average 60 percent less than other EU jurisdictions.

Malta has proven itself with a growing captive insurance and reinsurance industry. This is also thanks to its openly accessible regulator, which has been proactive in understanding the needs of the insurance business and embraces regulatory innovation.

What impact will the base erosion and profit shifting project have on captives and their need to return to Europe? This and more will be discussed at the New York captive conference. [CIT](#)

For sponsorship opportunities or to attend this event, kindly contact Anna Golis, research and development manager, on [agolis@pkfmalta.com](mailto:agolis@pkfmalta.com), or call us on +356 21 484 373.

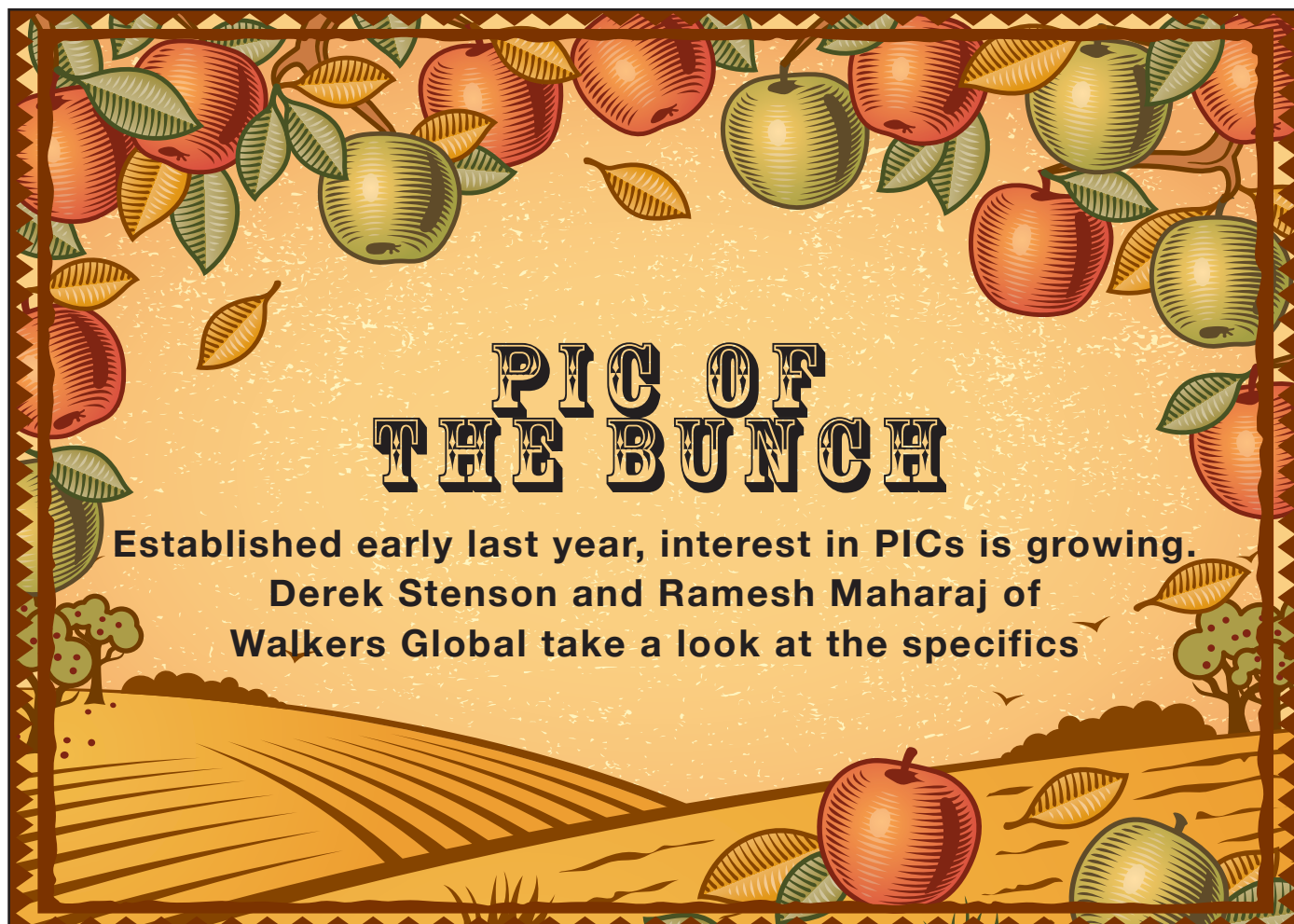


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Operating from Malta means utilising the freedom to provide services to companies that operate between EU member states, so captives can insure or provide insurance services to the vast European insurance market

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**Danielle Hermansen**, Director, PKF Malta



**Since portfolio insurance companies were introduced in the Cayman Islands in January 2015, have you seen a lot of interest in them?**

**Derek Stenson:** We have seen significant interest in the portfolio insurance company (PIC) product, which is not surprising given that the PIC initiative was insurance sector-led. The enabling legislation was specifically designed to allow Cayman Islands insurers established as segregated portfolio companies (SPC) to incorporate one or more of their segregated portfolios, also referred to as cells, as separate legal entities—PICs.

**What is a PIC's function? Do insurers need an SPC first?**

**Ramesh Maharaj:** The ultimate function of a PIC is the same as a cell of an SPC in that it permits the segregation of assets and liabilities of the PIC from those of the SPC itself or another cell of the SPC. PICs have a number of benefits, which may be attractive to some insurers. They are only available to Cayman-licensed SPC insurers, so to utilise a PIC an insurer must be established as an SPC or convert to an SPC, which is a relatively straightforward process.

**Under what circumstances should PICs be used and what are the benefits?**

**Stenson:** It will be a subjective test as to whether a PIC should be utilised or not. It is simply another choice on the menu of risk

management options made available by using a Cayman entity. When considering the establishment of a captive, or whether an existing insurer might potentially convert to an SPC, the pros and cons should be examined to determine if an SPC, which has the option of using PICs, is the most suitable structure for the captive.

The benefits of PICs are broad ranging:

- PICs can contract with another cell of its controlling SPC, or with the SPC itself (this was not previously possible);
- The risk of inadvertent comingling of assets among SPC cells is reduced;
- A PIC can have a different board of directors to that of its controlling SPC, thus allowing for greater governance flexibility;
- PICs have greater recognition from counterparties that are unfamiliar with unincorporated cells;
- They allow for easy transition to a standalone captive or insurer;
- An existing Cayman Islands insurer incorporated as an exempted company may utilise the PIC product by converting into an SPC;
- A non-Cayman insurer can re-domicile to Cayman, register as an SPC and then utilise the PIC product;
- Recognition as a separate legal entity for US tax purposes, allows tax elections to be made under its own federal tax identification number;
- Due to the fact that a PIC is a separate legal entity, PICs address a nagging concern with SPCs as to whether courts outside Cayman would recognise the segregation principles inherent in an SPC; and
- A single PIC can be wound up without affecting its controlling SPC or other PICs.

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PICs are an alternative to the more conventional legal structure of a captive

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**Derek Stenson**, Associate, Walkers Global



### What is the process to establish a PIC?

**Maharaj:** Each PIC will be incorporated as a Cayman exempted company and will be a subsidiary of its controlling SPC but related to a particular cell of the SPC. A cell can have no more than one PIC.

The insurance programme of an existing cell, including assets and liabilities, will be the subject of a statutory novation from the relevant cell to the PIC as part of a fast track registration procedure with the Cayman Islands Monetary Authority (CIMA). Although a PIC will be regulated by CIMA, with initial and annual filings and registration fees payable, it will not be separately licenced and instead will fall under the licence of its controlling SPC.

The incorporation of the PIC is simple and can be achieved within 24 hours. All the voting shares of the PIC must be held by the SPC but non-voting participating shares may be issued as required. The name of the PIC must include the letters “PIC” or “P.I.C.” or the words “Portfolio Insurance Company”.

Registration of the PIC with CIMA will be largely the same as the current procedure for creating a new cell of an SPC and will involve, among other things, the submission of an application with prescribed particulars, including written consent from the SPC, due diligence materials on proposed directors and officers (if different to those of the SPC), a business plan and the required filing fee.

If satisfied with the application, CIMA will issue a Certificate of Registration (no licence required) and the assets and liabilities of the relevant cell will be the subject of a statutory novation to the PIC. The PIC will have ongoing obligations to, among other things,

carry on its business only in accordance with the application submitted to CIMA, maintain a margin of solvency and capital in accordance with the requirements prescribed in the PIC legislation and make annual regulatory filings with CIMA.

**The cell concept seems to be rising in popularity. Do you see it overtaking the pure captive at all, or is it an alternative?**

**Stenson:** PICs are an alternative to the more conventional legal structure of a captive. The term captive covers a very broad range of insurers established for different reasons and to achieve different outcomes, which of course can change over time. PICs are simply a new option for these insurers to be utilised if they offer some benefit to the insurer or if they resolve a particular issue being experienced by the insurer. There is a place in the insurance sector for the various types of structures available, whether they’re single parent captives established as conventional limited liability companies or large SPC insurers utilising a significant number of PICs.

**How do they offer more flexibility in terms of quota sharing, risk pooling and reinsurance?**

**Maharaj:** For some SPCs, a drawback is that the cells do not have separate legal personality, which means that cells of an SPC, or the SPC and a cell, cannot enter legally binding arrangements, because of the absence of two legal parties. The result is that quota sharing, risk pooling, reinsurance or other arrangements between cells of an SPC is not possible. PICs have separate legal personality and so provide the captive the flexibility required to participate in these arrangements. **CIT**



“

The incorporation of the PIC is simple and can be achieved within 24 hours. All the voting shares of the PIC must be held by the SPC but non-voting participating shares may be issued as required

”

**Ramesh Maharaj**, Partner, Walkers Global



## Captives a-cooking

The Cook Islands has the ingredients to a be success, says Tamatoa Jonassen of the Financial Services Development Authority

### What is the state of the Cook Islands captive industry?

The Cook Islands recently created a captive insurance industry, beginning with legislation enacted in 2013. In 2015, the Cook Islands licensed its first captive insurer, and the 2016 outlook expects to see an increase in licences.

### What makes the Cook Islands an attractive domicile?

The Cook Islands is a well-established financial centre in the heart of the South Pacific. It is well known for implementing its innovative trust legislation in the early 1980s, which led to the modern asset protection trust, and which other jurisdictions have pulled from in an attempt to enhance their own financial service offerings.

The jurisdiction is able to combine the confidence of trusted service providers located in the Cook Islands with renowned insurance management services offered by multinational insurance companies

to tailor a captive insurance structure to a client's circumstances. As the Cook Islands are situated between Asia and the US, they gain the benefit of time zones, but they're also distinctively close to New Zealand and Australia.

The jurisdiction is well regulated with positive compliance ratings with the Organisation for Economic Co-operation and Development and Asia Pacific Group (APG). It is an independent country that is English-speaking, and was founded on common law, with a judiciary overseen by highly qualified New Zealand judges.

### What is new for the Cook Islands in terms of regulations, and is there anything on the horizon?

The Cook Islands recently had a successful phase-two peer review from the Global Forum. We are also expecting an APG review in 2017, which is anticipated to be just as positive as the last review, and the Cook Islands has committed to implement the Common Reporting Standards by 2018.

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The Cook Islands is a well-established financial centre in the heart of the South Pacific. It is well known for implementing its innovative trust legislation in the early 1980s, which led to the modern asset protection trust, and which other jurisdictions have pulled from in an attempt to enhance their own financial service offerings

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**What are your predictions for 2016? Do you think the captive insurance industry will grow in the Cook Islands?**

Most definitely. As a new product for the Cook Islands, it has no place to go but up.

There has definitely been a lot of interest shown towards this ‘new’ industry, with some prospective clients already expressing that they are keen.

**What is your strategy to increase interest in the Cook Islands captive insurance industry?**

The Cook Islands financial services industry has, over the last several decades, traditionally focused on the US market, with the Cook Islands international trusts having become the golden standard in offshore asset protection.

The Cook Islands has also tapped into the Asian market over the last decade and will continue to do so, especially with the increasing number of high net worth clients.

For captive insurance the Cook Islands’ initial focus is on the New Zealand and Australian markets, given the close relationship and proximity. But this product will also be suitable for clients from our Asian and American markets. **CIT**

**Tamatoa Jonassen**  
CEO  
The Cook Islands Financial Services  
Development Authority





# Industry Events

## CICA International Conference

**06-08 March 2016**  
**Arizona**  
[www.cicaworld.com](http://www.cicaworld.com)

The CICA International Conference 2016 is a great place to gather new ideas and expand your captive's horizons. You can network with captive owners, potential captive owners, risk managers, captive managers, domicile regulators and service providers.

## RIMS Annual Conference & Exhibition

**10-13 April 2016**  
**San Diego**  
[www.rims.org](http://www.rims.org)

This year's event includes more educational sessions, three inspiring keynote presentations, more networking opportunities and exciting events each day in the exhibit hall.



## People moves

### Comings and goings at USA Risk Group, Eurobase and more

USA Risk Group Barbados president **Martin Hole** has announced his retirement.

Hole has worked for USA Risk since the acquisition of MIMS International in 2008.

**Jeanne Crawford**, currently senior vice president at USA Risk, will take on this role and run the office in Barbados.

Eurobase International Group has appointed **Jonathan Moon** as group financial director.

Moon joins from PayPoint, a bill payment and cash collection service, where he served in various positions over a 19-year period, most recently as finance director.

In his previous role he was responsible for corporate and operational finance, planning and strategy, retailer debt procurement and facilities.

Moon commented: "I am very fortunate to be joining Eurobase at what is an exhilarating time in the group's evolution."

"I'm looking forward to applying my experience of driving efficiency and organisational change to support Eurobase's plans for continued international growth across all our divisions."

John Wilson, chairman and CEO of the Eurobase Group, added: "I am delighted that Moon is joining our senior management team."

"His wide breadth of experience and expertise in supporting businesses in the delivery of their strategic planning and business

reporting will be extremely valuable as we continue with our plans for further growth and expansion.”

**Kieran O'Mahony** and **Linda Haddleton** have been re-elected to their positions at the Insurance Managers Association of Cayman (IMAC).

O'Mahony will continue as chair of the association, while Haddleton holds on to her roles as vice chair and chair of the legislative and regulatory committee.

The new executive committee was elected at IMAC's annual general meeting on 20 January.

Secretary **Jennifer Reid**, forum committee chair **Erin Brosnihan**, research and development committee chair **Adrian Lynch**, scholarship committee chair **John Pitcairn** and marketing committee chair **JS de Jager** were all re-elected to their positions.

IMAC executive committee newcomers included **Jim Owen**, who was elected as treasurer, and **Colin Robinson**, who takes over as education committee chair.

**Seamus Tivenan** and **Stephen Gray** have stepped down from the executive committee.

O'Mahony commented: “I would like to thank both Tivenan and Gray for years of outstanding service to the Cayman captive insurance industry.”

“Whilst we will miss them on the executive committee, we are excited to welcome both Robinson and Owen and look forward to their contributions over the coming year.”

HAI Group has appointed **John Thomson** as its new president and CEO.

Thomson joins the public housing insurance agency from the Connecticut Insurance Department, where he was deputy commissioner. Thomson joined the department in 2012 to develop the new captive insurance unit. He was promoted to deputy commissioner in 2015.

Capstone Associated Services has promoted **Megan Brooks** to its executive management team as vice president of operations.

In her new role, Brooks will concentrate on team coordination and maintaining quality control.

She will work with Capstone's president and COO, Charles Earls, as well as CEO and general counsel Stewart Feldman, along with The Feldman Law Firm, in managing Capstone's operations.

Earls commented: “I look forward to continuing to work with Brooks in her new role.”

“This promotion is in recognition of her initiative and leadership, as evidenced by her work with Capstone over the last decade.”

In her new role, Brooks will continue to oversee the management and operation of property and casualty insurance companies, ensuring that any issues are addressed quickly.

Brooks said: “I'm excited to have been given this opportunity to help lead team Capstone as vice president of operations. I look forward to being a part of Capstone's continued success in 2016 and long into the future.” **CIT**

# CIT

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**If Captive Insurance  
is all about  
managing risk,**

then why put more  
risk in your captive?

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Domiciling your captive in Vermont means less uncertainty and more peace of mind. No headaches, no surprises, and no learning curve. With over 30 years of experience and over 1,000 captives licensed in the state, it's our higher standards that have made us the gold standard.

- Over 1,000 captives licensed
- 34-year history in captives
- 48 of the Fortune 100
- 18 of the Dow 30
- Nearly 100 healthcare-related captives
- Over \$170 billion held in assets

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