Leader of the pack

Bermuda's evolution from captive insurance jurisdiction to thriving re/insurance market has been accompanied by a host of regulatory developments. **Neil Horner** and **Natasha Scotland** chart the most important recent refinements in this area

The golden thread interweaving the fabric of the Bermuda insurance and reinsurance industry is its regulatory model. This is characterised by a facilitative but responsible approach towards regulation and continues to evolve.

The growth of the Bermuda market and its accompanying regulatory developments certainly merit close inspection. Recent highlights include the important changes introduced by the Insurance Amendment Act, 2006, as well as the proposed new risk-based capital model (RBC) for the Class 4 companies.

A MARKET LEADER

Rating agency AM Best's 2005 report provides some significant information regarding Bermuda's insurance and reinsurance market position. According to this report, Bermuda held 15 of the top 35 reinsurers in the world, ahead of Europe, which had 11.

Also, according to AM Best's *August 2006 Report P/C and Life*, Bermuda is ranked as one of the top five insurance domiciles behind US and Germany, having one of the largest property cat reinsurance markets and supplying 40% of the US market.

Additionally in *Profiling the Bermuda Captive Market*, published in the Bermuda Captive Conference edition September 2007, Dr Marcelo Ramella, assistant director of research at regulator, the Bermuda Monetary Authority (BMA), provided a detailed analysis of Bermuda's

global position in the captive insurance market. According to Dr Ramella's report, Bermuda maintained its status as world market leader with US$19.4bn in gross written premium for 2005, which was three times as much as its closest competitor, the Cayman Islands which itself wrote US$6.7bn in the same period.

Captive insurers remain the bread and butter of the Bermuda insurance market but Bermuda has also become the jurisdiction of choice for the highly capitalised property catastrophe Class 4 reinsurers. It is critical that Bermuda continues to develop its regulatory model appropriately and responsibly to ensure it is in line with best global practice. And Bermuda is indeed doing just that.

IN CONTROL

An important change introduced by the Amendment Act is the concept of a 'controller' and the requirement that any person planning to become a controller of an insurance company must give notice to the Bermuda Monetary Authority.

The definition of a controller includes a managing director or chief executive of an entity registered under the Act. The 'shareholder controller' requirement under the Amendment Act is particularly noteworthy as no person can become a shareholder directly or indirectly of 10%, 20%, 33% or 50% of the voting shares of an insurance company unless prior notification has been given to the BMA.

The BMA must then inform the company that it has no objection or 45 days must lapse since the notification was given.

If the insurer is a public company, written notification must be provided to the BMA within 45 days of the person becoming a shareholder controller. Alternatively, if the insurer is a private company, the prospective shareholder controller must notify the BMA of his intention to become a shareholder controller. The potential shareholder must not become a controller unless he has been notified within 45 days from the date of service that the BMA has no objection or the BMA has not served a notice of objection within the 45 day period.

The BMA may serve a notice of objection on a potential shareholder of the private company and must be satisfied that the person concerned is a fit and proper person to become a controller of the description in question of the insurer. It must also be satisfied that the interests of clients or potential clients of the insurer would not be threatened by that person becoming a controller and that having regard to that person's likely influence on the insurer as a controller the minimum criteria would continue to be fulfilled in the case of the insurer or if any of those criteria is not fulfilled, that the person is likely to undertake adequate remedial action.

The Amendment Act also establishes an appeals process which can be invoked if, for example, any party is dissatisfied with a BMA objection to a person becoming a controller.

These amendments further serve to strengthen the insurance regulatory framework in Bermuda and are to be welcomed. They have been accompanied by significant reform to Bermuda's underlying company law framework.

STREAMLINED PROCESS

The BMA has recently issued a notice on the separation of the incorporation process for insurance companies. Previously, in order to incorporate an insurance company, documents had to be simultaneously submitted relating to the licensing of the entity under the Act, as well as company incorporation documents under the Companies Act 1981. The BMA has now streamlined the process and can review applications for the incorporation of the company separately from applications for registration of insurance companies. It is important to note, however, that approval of a company for incorporation is not an indication that an application for the registration of the company as an insurer will also be approved. As the incorporation and licensing ▷

processes are actually dealt with by two separate divisions within the BMA, this two-stage incorporations procedure is more practical and offers greater flexibility.

RISK-BASED MODEL

Bermuda has always had a risk-based approach towards the regulation of its insurers and reinsurers. This is demonstrated by the 'class-based' approach which divides Bermuda insurers and reinsurers into four classes. These range from a Class 1 captive insurer through to a Class 4 property catastrophe reinsurer such as Ace or XL.

The current capital requirements for Class 4 insurance and reinsurance companies call for the maintenance of minimum solvency margins. This means maintaining a minimum solvency margin requirement greater than $100m; 50% of net premium written, with a partial deduction for credit for reinsurance; or 15% of loss reserves.

In July, 2007 the BMA issued a consultation paper on internal models which set out the BMA's proposals on the use of company-specific internal models to assist in determining a company's regulatory capital requirement. In this consultation paper, the BMA indicates its intention to introduce the Risk-Based Capital (RBC) Model in determining an insurer's regulatory capital requirement and its belief that an insurer's risk profile should determine its capital adequacy. The BMA proposes that where the insurer believes that its own internal model better reflects the inherent risk of its business, it can apply for approval of its internal model to be considered in the determination of its regulatory capital requirement.

The RBC Model further refines the insurance and reinsurance regulatory framework in Bermuda as it looks to the particular risk profile of individual companies in making an assessment of its capital requirements. The insurer's risk profile includes the quality of its management, corporate governance, the inherent risk of its business and how it mitigates those risks. It is important to stress however that Bermuda has always had a risk-based approach towards insurance regulation.

This capital adequacy assessment tool, alongside the on-site programme for Class 4 insurance companies, which was introduced in 2005, serves to highlight Bermuda's continued efforts in relation to the supervision of insurance companies. The on-site programme includes on-site meetings with the senior management and related staff at each company. At these meetings, the insurer's strategic initiatives, alongside any developments within the organisation and factors that are affecting or concern management are a few of the items which would be discussed. These meetings continue to be an effective tool in the BMA's regulatory arsenal.

IN STRONG SHAPE

Bermuda has created a business environment that nurtures and sustains free enterprise, supported by informed and appropriate regulation and necessary infrastructure. Through continued enhancement of its regulatory infrastructure, Bermuda is able to maintain appropriate supervisory controls over the insurance and reinsurance sectors. It appears that Bermuda is well equipped to deal with future developments in international standards in the insurance and reinsurance industries. The continued refinement of the regulatory framework of Bermuda will support the next phase of growth and will allow the island to preserve its appeal as a credible and leading insurance and reinsurance jurisdiction. ®