LATAM REPORT 2015

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CAPTIVE REVIEW

EDUCATION
New industries discover efficient captive solutions

REGULATION
Institutional support required throughout Latam

COMPETITION
Offshore domiciles competing for growing Latam business


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Introduction

The Latin American captive insurance market is enjoying a significant boom in business as more regional industries become aware of the advantages a captive can offer.

Offshore domiciles such as Bermuda, the Cayman Islands and the British Virgin Islands are enjoying an upsurge in interest from the region's businesses seeking to write diverse lines of insurance such as health, energy or catastrophe.

However, Latin America as a region is vast with huge disparity in the types of industries seeking solutions across the countries.

Colombian and Mexican organisations are widely regarded as frontrunners in establishing captive vehicles, while Venezuela and Brazil seem to be slower out of the gate.

Captive Review speaks to industry experts from both inside and outside of Latin America who discuss the overall optimism and the healthy appetite for captives.

At the same time they point to a chronic lack of information on captives in the region and the absence of established regulatory bodies as the biggest hurdles the industry has to face in the coming years.

We analyse all these key points and more within *Captive Review*'s *Latam Report 2015*.

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CAPTIVE EFFICIENCIES COMING TO LATAM

Rainmaker Group CEO Gabriel Holschneider explains how the captive industry is shaking up the status quo in Latam's insurance market for the better

Captive Review (CR): What is the overall outlook for captive insurance in Latin America?

Gabriel Holschneider (GH): The overall outlook for captive development is fantastic but penetration is not where we would like to see it yet. Large multi-Latin corporations that are privately owned have really developed an appetite for captive insurance and they are asking more and more questions about how they can engage in a captive insurance strategy.

On the other hand, regulation is not up to par. There is a lot of work to be done regarding regulation in most Latam jurisdictions; if not to admit captives then at least to recognise them. It's one thing to have legislation in place to recognise captive insurance as a local solution for risk retention, and another for jurisdictions to acknowledge the use of captives as common practice.

The overall outlook is very positive but at the moment we are only scratching the surface of the potential of the captive insurance industry in Latin America.

CR: Is the regulatory shortfall being addressed?

GH: There is an awareness in some jurisdictions but it doesn't seem to be a priority yet. There is a lot of market buzz about captives but also a lot of ignorance surrounding their purpose and nature. This ignorance has caused brokers and seeding companies to be fearful that captive formations will eat away at their core business. I'm not sure the market hype is being translated by governments from an academic or political responsibility perspective at the moment.

Written by **Gabriel Holschneider**

Gabriel Holschneider is the founder and president of the Rainmaker Group. His trajectory in the insurance field has proven that there is broad opportunity for global programs to find innovative, transparent, and efficient risk-transfer solutions. Prior to founding Rainmaker, he worked as legal and financial consultant in private equity, commercial arbitration and international transactions designing corporate structures.

If you compare the Latam framework with the US market, which is very robust and mature, you can observe that Latam should be mimicking a lot of these steps the US previously took, such as forming an association of captive managers or captive owners. There is no real representative for this sector at the moment and it could help open up our criteria for legislation in the region. As an industry we should be focusing on bringing captive managers, owners and advisers together and representing them as a whole.

CR: How would you rank the Latam countries in order of their captive industry sophistication?

GH: Colombia firstly is very proactive and Panama is also setting a strong standard. Mexico is arguably third and the rest of the region all fall in behind that.

CR: What are the chief drivers for growth and implementation of captives in Latin America?

GH: Primarily the driver is the economy and economic maturity. Also, there is a lot of room for greater efficiency within the entire Latin American insurance sector.

Clients are driving the industry because they now know they will gain efficiency and find captives a more agile and dynamic way to run their risk. They are more sophisticated – they get it now. They are more in touch with the English language and are talking with business associates abroad and discovering how well captives work there.

> **"The overall outlook is very positive but at the moment we are only scratching the surface of the potential of the captive insurance industry in Latin America"**

CR: How important is this increasing international contact with other English-speaking markets?

GH: At the moment captives are an under-valued opportunity in Latam. But corporates are looking to their neighbours to the north to see how they can become more efficient in all aspects of management. Client are increasingly employing MBA or PHD graduates who have studied abroad and have US or European industry contacts who can share different aspects of how foreign insurance business operates.

Latam is doing very well if you consider the economic scale these countries. These are still insurance sectors that are undergoing development and are very immature. They still have to broaden the base of insurance products available to the general public and create a culture of insurance services among consumers.

CR: Which industries or businesses in Latin America are already taking advantage of the benefits behind captive insurance?

GH: All corporates or industries that have catastrophic risk exposure. No one suffers more from the hard and soft reinsurance markets than catastrophic exposures, which has led these companies to keenly look at captives as a long-term strategy that will allow for significant saving.

Secondly, there is a growing interest on the liability side from companies that have massive distribution channels. These firms are looking to use companies as a profit centre because they have the ability to displace the product. Instead of giving that business away to a local seeding company, they can participate in the profitable business.

Finally, the entire energy market is also very excited by captives. This goes from state-owned corporations through to small drilling contractors or any kind of energy-related contractors. This is because the US and Europe have done such a magnificent job of leveraging captives for energy risk; anyone who's anyone in the energy market uses captives.

There is a lot of appetite from large entities who want to access the market at a wholesale level and stop engaging a retail level, which is very inefficient. However, here in Latam, government agencies are hesitant and are still paying huge sums of money through regular retail channels.

CR: How are captives being utilised by the Mexican government entities to offset country-risk?

GH: My experience is that they are eager to develop a mechanism to establish a direct relationship with the reinsurance market at a wholesale level. At the moment the Mexican Government buys its insurance at a retail level which is very expensive. It is interested in developing economies of scale which is essentially approaching the reinsurance market as a whole, as opposed to having each government entity tender its processes individually. A captive may very well be the key the government is looking for to help represent their collective assets in an orderly fashion.

"For those of us who are trying to push captives in Latin America it has been somewhat of an uphill battle because there is a lot of resistance from the traditional insurance market"

In addition, the government is also interested in developing a captive to work as a profit centre. It can grow into a very robust treasury, which is something CFOs and CEOs are obviously very interested in. It's about savings and access, harnessing your own risk and making benefits from it while surfing the hard markets with a vehicle that allows you to balance your budgeting.

CR: Should all Latin American governments be looking at captives?

GH: Absolutely. There are already several government agencies that want the efficiencies of a captive.

CR: What are the greatest challenges facing the development of captives in Latin America?

GH: Captives are fantastic for clients but very disruptive in nature because they upset the status quo for brokers. For those of us who are trying to push captives in Latin America it has been somewhat of an uphill battle because there is a lot of resistance from the traditional insurance market.

Clients can enjoy a captive from day one, but from within the industry it causes a lot of upset for anyone who benefits from the current system. The transparency and the no nonsense approach to risk leaves little room for shady commissions or back-door and retro agreements, which is very uncomfortable for a lot of people.

Currently, insurance carriers throughout Latam have put themselves in a very comfortable position, alongside the brokers, where they offset the majority of their risk into the reinsurance market. Large insurance companies are actually just feeding their risk into the international markets as it still brings in commission and has no inherent risk. This causes a very cumbersome process and over-intermediation, whereas captives provide a very streamlined solution to risk.

The major reasons why Latam businesses haven't been introduced to captive solutions before are a combination of ignorance from their point of contact or outright fear that captives will undermine commissions.

Ultimately, the three issues are ignorance, fear and a lack of an integrated regulatory system. The answer is that those of us who are interested in making captives grow need to come together as an association to invest in sharing how captives can benefit Latin American jurisdictions.

LATAM'S EMERGENCE HAS CAPTIVE AUDIENCE

Gus Frangi, global business development manager at AMS Financial Group, offers an overview of the key features underlying the development of the Latin American captive sector

Recurrent references to the potential development of captives across the region have become a constant feature of discussion and there is indeed a great deal of factual evidence underpinning this argument. Our knowledge of the Latin American market and the consistent rapport that we entertain with relevant operators enable us to make an objective assessment devoid of simplistic assumptions. From a generic standpoint, the change in the fortunes of this vast economic space is palpable. Long gone are the days when foreign investors associated political and economical turmoil to Latin America. However, the transformation achieved by the region has been far from homogeneous and vast differences prevail between countries. Despite ostensible intraregional divergences, the advancement of a consistent assessment from which valid conclusions could be drawn should focus on underlying trends. Of special relevance is the implementation of innovative government policies in the major regional powers, which have gone hand in hand with a positive evolution in corporate governance.

It is clear that none of the region's remarkable achievements in macro and micro economic terms would have been reached, had it not been for a conscientious decision of the regional leadership to embrace globalisation. This has not been a concerted effort but rather a process of natural progression undertaken by each country in response to specific needs and aspirations. There is, for example, a clear difference between the policies for economic development pursued by nations such as Brazil and Mexico versus those implemented by Colombia and Peru. Casting differences aside, these policies have been effective conduits to increase the foreign investment flow. With a market of 550 million consumers, a gross domestic product equivalent to a third of that of the US, an expanding middle class and a strong reliance upon dynamic foreign, financial and services sectors, Latin America has attained a degree of maturity that warrants the need for sophisticated insurance products. Within this backdrop, the development of Latin American owned multinational conglomerates has been a contributing factor to the demand for new insurance products.

Written by
Gus Frangi

Gus Frangi, global business development manager, AMS Insurance Management Services Limited joined AMS in 2012 with a mandate to build up key relationships and partnerships. Frangi has over 20 years of experience in the international insurance and reinsurance industry, having started his career as insurance manager for Esso in South America.

Looking ahead, the ongoing slowdown in the commodity prices is bound to affect the regional economic performance that should fall short of that of the leading industrialised nations in the short term. Despite this change in gear, nothing seems to foretell that the region is heading for an abrupt reversal of fortunes having undergone robust processes of economic reform. This tough environment is, however, bound to put pressure on service providers, forcing them to enhance the quality of their captive offering across the region.

The framework for captives across Latin America

It is a well-known fact that the regulatory frameworks foisted upon the insurance industries across the region have not kept pace with the needs of an ever more discerning clientele. Despite this state of affairs, international underwriters and service providers have been flocking to Latin America for decades, bringing substantial levels of capacity and innovative products along with their own know-how that, in turn add up to the highly skilled pools of local professional resources.

Most jurisdictions across the region remain 'admitted' territories where the introduction of alternative risks transfer vehicles is far from being encouraged. While the impact of regulatory restrictions cannot be accurately quantified, the circumstantial evidence suggests a limited dissuasion as clients have not been deterred from setting up captives elsewhere. Nonetheless, the barrage of regulatory limitations has led to the development of convoluted operational layouts. Latin American businesses purchase insurance coverage from admitted local carriers who in turn reinsure through admitted channels. As most national insurance legislations do not tolerate the introduction of non-admitted vehicles, captives must operate as reinsurers that take up retrocessions from admitted reinsurance carriers. This is hardly conducive to efficiencies. In some territories like Argentina and Venezuela there are added regulatory complications, posed by restrictions to the free flow of currency.

The national regulators' lack of exposure to captive solutions presents a further disadvantage, as only a handful of captives are registered in their home domiciles. In most cases, the registration with the relevant financial regulator is a painstaking process relying upon the rating of the captive by a recognised credit agency.

Regional regulatory harmonisation could help propel the financial sector, with a direct impact upon captives. The facts demonstrate that the region is far from attaining effective levels of transnational consistency. It is, however, important not to lose sight of some revealing facts. The enactment of Article 61 to Law No 1328 in Colombia, easing the requirements for insureds keen to purchase cover overseas for risks not deemed compulsory is an auspicious landmark. Yet despite limitations, the trend points at a 'progressive' modernisation of the otherwise outdated regulatory frameworks, along with a better perception of the inherent benefits that captives bring about.

Preferred destinations for Latin American captives

At the outset, Latin American organisations that embraced captive solutions were large conglomerates. However, as the economy took off, captives progressively cast their spell across a broader corporate spectrum. The regional entrepreneurial culture is fast evolving and patriarchal structures are being phased out and replaced by modern corporate layouts that rely upon good governance and technical innovation. It is therefore a matter of natural progression for captives to find a stronger foothold in the region.

For decades, the key captive domiciles have catered for North American and European business, paying limited attention to Latin America. Only recently there has been a shift in attitude underpinned by a string of factors that impacted upon an otherwise narrow approach.

Here are a few points to understand this trend:

- The Foreign Account Tax Compliance Act (Fatca): the Federal law that requires US persons, including those who live outside the United States, to report financial accounts held outside of that country. This law applies to foreign financial institutions.
- The increase in the number of US jurisdictions prepared to underwrite captive business emanating from within the US, avoiding the complications associated to Fatca.
- The Non-admitted and Reinsurance Reform Act of 2010 (NRRA), part of the Dodd-Frank Reform and Consumer Protection Act, stipulating that non-admitted insurance is subject to the statutory and regulatory requirements of either the insured's home state or, when the insured risk is located elsewhere, the state to which the greatest percentage of the insured's taxable premium is allocated.
- The Solvency II EU Directive with provisos on capitalisation held by insurers. The attempts by some captive domiciles to enact equivalence provisos and retain a degree of symmetry with the premises of this directive have been vastly publicised; the directive, however, is yet to be implemented. Whereas it is commonly agreed that the application of the directive's pillars to banking and insurance adheres to the principles of financial prudence, good governance and transparency, there is recurrent debate about its transposition to the captive industry.

These developments have fuelled the interest in Latin America among several captive domiciles that see in the region an avenue for growth. An overview of the jurisdictional responses to the challenges posed by the newly found regional confidence reveals a broad offer of domiciles well suited to address the needs of the regional clientele. Over the years, Latin American captives have shown an understandable preference for domiciles within regional reach. However, some captive owners have looked further afield, having chosen European jurisdictions.

Among the domiciles with a solid interest in the region, we remark the sustained efforts of Barbados re-affirming its credentials as a jurisdiction of choice for Latin American business. Barbados has been a prominent captive domicile in its own right for over three decades, boasting world-class legislation, a robust body of law that recognises the precedent of the English Common Law, an autonomous and highly regarded financial regulator and a sophisticated financial services sector. The jurisdiction is ranked among the world's top 10, being home to 230 captive insurers that write $30bn worth of annual premiums. Barbados' risk span is broad, encompassing property and casualty, motor, professional risks, products and directors & officers liabilities, to name a few. There is no restriction for writing of emerging risks.

"The regional entrepreneurial culture is fast evolving and patriarchal structures are being phased out and replaced by modern corporate layouts that rely upon good governance and technical innovation"

Like the rest of the captive domiciles in the Caribbean and mid-Atlantic, the bulk of Barbados' client base emanates from North America. However, the jurisdiction has been a pioneer in the negotiation of bilateral agreements for the avoidance of double taxation and investments with various regional jurisdictions like Mexico, Panama, Venezuela and Cuba. Barbados has staunchly defended the right to use the bilateral mechanisms to the detriment of multilateral instruments. Barbados' reputation as a world-class jurisdiction keen to uphold a renowned international co-operation regime for the exchange of tax information is broadly acknowledged. Its own gravitas along with a remarkable pool of professional resources draws the attention of Latin American clients. This consistent regional approach is bearing fruits, new formations are using Barbados and existing ones have redomiciled to Barbados.

Conclusion

It would be naive to expect the development of Latin American captive business to be an easy proposition. For all the intricacies and barriers facing prospective clients, the region should continue to witness a consistent development of its home-grown captives. Opportunities abound and the appetite for captive solutions continues to grow.

LATAM AND THE CAYMAN ISLANDS – NATURAL PARTNERS?

Andrew Cater, senior underwriter with United Insurance Company, explains the history of the Cayman Islands' relationship with Latin America and what to expect in the future

In the beginning was Christopher Columbus.

Circa 513 years ago Columbus quietly stumbled upon and named these islands 'Las Tortugas' after the huge numbers of Turtles he observed. The Cayman Islands or 'Las Islas Caiman' title came later once other explorers also discovered the huge number of Caiman here. A Caiman, according to Wikipedia is 'an alligatorid crocodilian belonging to the subfamily Caimaninae, one of two primary lineages within Alligatoridae, the other being alligators'. The place was full of them apparently.

Is this yet another tenuous link with Mr Columbus being claimed by yet another territory to enhance and advance its mutual links and heritage with parts of Latin America?

Written by
Andrew Cater

Andrew Cater is a senior underwriter with United Insurance Company, a Cayman based reinsurance company managed by Aon Cayman, that provides bespoke reinsurance solutions to Aon managed clients worldwide.

Apparently not. Again, the wonders of Wikipedia and other research would indicate that he really did see and name these fair islands on 10 May 1502. And, of course, he also discovered large swathes of what is known these days as Latam.

> "Circa 513 years ago Columbus quietly stumbled upon and named these islands 'Las Tortugas' after the huge numbers of Turtles he observed"

The here and now

I shall not go through the entire history of the Cayman Islands and the other links to Latam. However it is clear that geographically, historically and now economically Cayman is, and will also be, inexorably linked to Latin America. Apart from the captive insurance industry that you as readers of this report will be aware of, few people realise the other connections that Cayman has with modern day Latin America.

For example, through the multitude of captive managers, reinsurers, law firms, accountants, auditors, actuaries, fund managers, the 210 current banking licences and host of other service providers, Cayman somewhat surprisingly is the fifth largest financial centre in the world, and second largest in the Western Hemisphere after New York. Most would never have even contemplated that the majority of Latam's infrastructure development is being funded via Cayman, a true claim that no others can match. Nor that great advice is given on structures and ownership arrangements. The reasons Cayman has reached such an elevated standing are clear – great infrastructure, great services with world class staff, a neutral tax environment where all players are equal, and above all a British overseas territory where the ultimate court is the Privy Council in London. All of that in islands with a 59,000 population.

In the captive world, while Cayman is not quite as noisy in the press as its counterparts in Bermuda (something that is in the process of changing) we already have an impressive 24 full captives of Latam origin domiciled here with combined assets (as of December 2014) of $1,24bn and annual premiums of $285m. In addition, whilst full figures were not available at the time of going to press, I am personally aware of another 23 segregated portfolio companies with an approximate worth of $1.2bn of Latin American origin.

Indeed, here in United Insurance Company (for those who do not know, it is the only reinsurer with an A.M. Best rating of A- , which uniquely provides reinsurance and other services to captives) we have seen our written premiums grow from almost nothing in 2012 to around $8m now and still growing. We see opportunities in all areas in Latam that we are involved in and where we are currently licensed as a reinsurer, be that pure reinsurance on either a quota share or excess loss basis, stop loss of clients captive retentions, acting as fronting reinsurer where allowed. Our clients are increasingly sophisticated buyers and see the structures we are able to build with them as assisting them in meeting their goals.

I travelled to Colombia twice in 2014, as well as Chile and Argentina, all with promising results and tremendous interest generated in the Cayman domicile for reasons expressed above. On one of my Bogota trips, I was lucky enough to be joined (in a seminar organised by Aon Bogota on the subject of the Cayman domicile) by representatives of the Cayman Islands Government, PwC, Maples law firm and RBC. Our audience of 80 or so business people, and indeed we all as speakers, were highly impressed by Cayman Islands Government's (CIG) decision to send a senior figure in support of its finance industry. This is indicative of the view that CIG takes on supporting its economy, entering into the appropriate tax agreements and so on with other governments to ease the path of business, and I am aware that CIG has similar plans to continue that activity in future. What was even more impressive was the seamless presentation we all worked hard to put

together to showcase the multiple talents and deep infrastructure that Cayman has to offer.

We have identified Ecuador, Peru and Mexico as additional places of interest for 2015, certainly as far as our business is concerned, and will be doing our best to obtain reinsurance licences in those countries.

When we look at other areas it is quite clear that non-financial service industry businesses are also seeing the opportunities and feeling

"When we look at other areas it is quite clear that non-financial service industry businesses are also seeing the opportunities and feeling the increase in business between Latam and Cayman"

the increase in business between Latam and Cayman. There are new direct flights planned between Cayman and Colombia, Costa Rica, Panama, Mexico, Dominican Republic, amongst many others. Currently most travel has to be arranged via Miami, and so these routes will save travellers from those countries a huge amount of time and inconvenience in having to transfer planes. More hotels are being built to accommodate ever increasing numbers of not just business visitors but Latam tourists. Spanish is now frequently spoken and heard in the fine bars and 150 or so high class restaurants of Grand Cayman.

All this is fantastic news. However, I for one cannot lose sight of the fact that other domiciles are making great strides too and Cayman should not become complacent of its current lead in the area. We must all (and not just Cayman) also recall that while our Latam client bases are growing with increasingly sophisticated buyers, we must spend time and money investing in the education of potential clients not just about what the captive industry is, but also what it is not. A great deal of attention must be paid to the KYC, due diligence, AML, ownership structures and other factors to avoid any misunderstandings that could at some point lead to embarrassments for our clients or for us as an industry. We must continue to deliver news on the latest developments, in terms of both products and compliance to ensure they receive the best advice and are able to act accordingly.

In summary, the historical links in the 'founder' of Cayman and many Latam territories all those years ago, the close geographical proximity and increasingly good connections, the willingness and experience of the people both in Cayman and Latam in having done and doing business now, I think bodes well for the future. As previously expressed, the huge volumes of not just captive business but finance and other projects really do make Cayman a natural choice of domicile for Latam.

Oh, and by the way, the Caiman have gone. Just turtles left.

COLOMBIAN CAPTIVES EXCEL WITH BERMUDA

David Gibbons, managing director and captive insurance leader at PwC Bermuda, and Carlos Chaparro, partner at PwC Colombia, discuss why Colombian captives are flourishing

Written by **David Gibbons**

David Gibbons is managing director and captive insurance leader at PwC Bermuda. He leads the captive insurance group and has more than 14 years' experience in the insurance industry in Barbados and Bermuda.

Written by **Carlos Chaparro**

Carlos Chaparro has been a member of PwC since 1995, Chaparro is a tax partner based in Bogotá with extensive experience in corporate and individual tax. For several years he was a member of the International Assignment Solutions practice in Colombia.

Captive Review (CR): Why is now the right time for Colombian companies to open a captive?

David Gibbons & Carlos Chaparro (DG&CC): Colombia is an attractive country for insurance and captive insurance companies, with GDP growth of more than 4% per year for the past three years, continuing almost a decade of strong economic performance.

One of the main driving forces being the evolution of 'multi-Latinas' in Colombia and Latin America over the past 10 years. Their aggressive expansion across the Americas has led to a pattern of greater sophistication in the insurance market as noted by the number of insurance policies written. As Colombian multi-Latinas continue to grow beyond their country's boundaries, they are increasingly more focused on the risks they need to manage and are actively pursuing cost-efficiencies. This has resulted in an increase in demand for insurance that exceeds Latin America's overall economic growth and has resulted in robust premium growth across all Latin American countries, with Colombia's premium growth at 8% in 2013.

Specific insurance products and market segments with high growth potential in Colombia and Latin America include personal lines and life insurance. Insurance regulation in Latin America is evolving towards a more sophisticated risk-based capital approach to solvency assessment. This is in line with European and US regulatory trends, and more open markets in the Pacific Alliance countries of Chile, Mexico, Peru and Colombia.

In the natural evolution of a multi-Latinas, there is a point where there are several separate cost centres either locally (e.g. Cali, Bogota, Medellin) or regionally (e.g. Colombia, Peru, Chile) for which there is often the possibility of the insurance coverage for each centre to be inconsistent with the group overall. Thus, it is important to centralise the risk management and insurance purchasing process. A key part of this is a detailed understanding of the amount of risk sitting within the organisation. A captive acts as a home for this self-insurance and necessitates a focus on a centralised insurance process.

CR: What are the tax implications of opening up a captive in Bermuda?

DG&CC: Bermuda has signed new international agreements with 50 other nations which allow automatic exchange of financial information which has been backed by the Organisation for Economic Cooperation and Development (OECD) and the G20 group of leading economies. The OECD points to the strength of Bermuda, stating that, 'Bermuda's exchange of information practice is in line with the international standard of transparency and exchange of information for tax purposes'.

The continued commitment to Latin America has been strongly supported by the authorities in Bermuda, with the signing of 45 tax information exchange agreements (TIEAs) and more than 60 multilateral agreements. Of the TIEAs signed, five have been with Ibero American countries, namely, Argentina, Brazil, Colombia, Mexico and Portugal, and negotiations completed with Chile and Spain.

From a Colombian perspective, the tax treatment has remained unchanged for a number of years. Captive insurance companies are generally not subject to direct taxation provided the captive insurer does not have a permanent establishment, or its effective place of management in Colombia. At the same time, deductibility is generally available, although capped at 15% of the resident's taxable income net of this expense, as well as insurance costs need to be arm's length. Most insurance services are subject to VAT at 16% which is collected and remitted through reverse charge rules by the resident party when it comes to non-resident captives insuring into Colombia. The absence of tax consolidation also offers opportunities in terms of captives actively participating in the international capital markets, without immediately attracting taxation in Colombia.

Moreover, on 7 October, 2014 the Organisation

of Taxes and National Customs of Colombia (DIAN) issued resolution N.8388 of 2014, which certified that certain jurisdictions mentioned in Decree 2193 of 2013 would be allowed to exchange tax information with Colombia, Bermuda being one of those jurisdictions. In addition, regulation 1966 of 2014, Colombia's blacklist, does not include Bermuda and any information exchanges will be subject to confidentiality rules and other safeguards as part of another convention on tax matters.

CR: What types of insurance are Colombian captives writing?

DG&CC: According to Superintendencia Financiera de Colombia, owing to strong economic growth over the last decade, Colombia now boasts the fourth largest insurance market in Latin America, reaching GWP of $4.5bn in 2014. In Colombia's non-life market the most important line of business is automobile and P&C insurance representing approximately 40% of the non-life market.

Colombian captives are typically writing either business which is sitting as deductibles for insured cover already on the organisation's books such as property, or writing cover that is very specific to the company and thus cannot be placed in the market or would be placed at an abnormally high rate (e.g. surety bonds and contractual liability).

CR: What are the first steps for risk managers in setting up a captive?

DG&CC: The risk manager should understand which risks should be placed in the captive and how much capital would be required to cover that risk. If multiple risks are identified it is often easier to adopt a phased approach to bringing these into the captive. The risk manager then should work with their broker to fit the captive into their current insurance/reinsurance structure as fronting to the captive is usually required. Also taking advantage of the fronting insurer's claims management process is a real advantage especially when the captive is in its infancy. These are the fundamental parts of a feasibility study.

CR: What are the next steps?

DG&CC: The main undertaking for managers and shareholders is to fully understand the concept of a captive and the benefits it provides. Other items to address are the fronting possibilities and ensuring the business selects the best fronting company for their risk and location. Regulation is also an aspect one must consider as each Latin American country's regulation is unique. Establishing a captive and understanding the various applicable country regulations can seem complex, but the benefits captives bring can justify the effort.

Despite the presence of the tax agreements in place, individual tax positions vary from company to company and tax advice should always be sought to understand the implications in both Colombia and the captive domicile. As fiscal pressure mounts, it is likely that tax laws will change with great frequency and therefore active monitoring of the regulatory environment is critical to ensure compliance and adequate reaction to changes.

Once a domicile has been selected (domicile analysis is usually also part of the feasibility study) and the business plan is being prepared, it is important to involve all relevant service providers (e.g. lawyers, auditors, account managers) in this process as they have will have a full understanding of regulatory requirements and can assist with early interactions with all relevant regulators.

OFFSHORE DOMICILES FEEDING THE CAPTIVE FIRE

Maria Escobar of Marsh talks to *Captive Review* about how the whole of Latin America has developed and the part offshore captive domiciles have to play in its future

Written by
Maria Escobar

Maria Escobar is the head of Marsh Captives Solutions for Latin America. She is responsible for the market development in the region and the coordination and delivery of Marsh captive capabilities throughout the region. Escobar articulates for LatAm clients the overall Marsh global captives solutions to offer the best products and adviser to Marsh clients.

Captive Review (CR): How has Latin America, as an emerging market, developed in the last year?

Maria Escobar (ME): Latin America is facing an interesting change in terms of risk management. As an emerging market with sustainable growth over the past years, it has become more integrated and more sophisticated regarding risk financing options and now has the perspective to understand and take advantage of the 'positive' side of risk. Considering the size of the region and the different development levels of the countries, there are obviously some countries that are more advanced and open to analysing new options and alternatives to leverage the total cost of risk for their companies. The global nature of some of the companies, and the need to be competitive in a global environment, has pushed them to review their peers' strategies in terms of risk optimisation and the most efficient way to participate in a more active way in the risks they face. They are changing from a 'passive' attitude to a more proactive approach, recognising the opportunities they have when they understand and take more control of their risks.

Although the risk manager role is still 'under construction' in Latam, some important companies have begun taking the first steps to incorporate the role at an appropriate level into the company. These companies have also taken a more strategic view, understanding the benefits of an enterprise risk management approach linked with the bottom line of their financial results. There is still a long way to go, but we are seeing some awareness among directors about how important the role will become.

On the other hand, Latam has been experiencing important growth in the middle class over the past years, which has had a positive impact on the dynamics of regional economies and created positive financial results for some companies. Those firms are now expanding their operations and are in a better position to retain risk, not only because of the availability of cash flow, but because they are confident in their knowledge of their risks.

CR: What sort of companies are showing interest in forming a captive?

ME: We are mainly seeing interest from large corporations with representative presence in their country and some with important operations abroad. These companies can be from the private or public sector. Most of them have been very traditional in their insurance programme structures and some of them even have self-insurance funds. What a captive solution can offer them is a more efficient way to structure their insurance programme and to manage their retentions. The first step is to help them understand the benefits of integrating a captive into their risk financing strategy and how this can be built upon in the future.

There are also mid-size companies, especially from the private sector, that are interested in captives. Because they are already retaining part of their risk, a captive can work as a tool to efficiently manage this retention and leverage the company´s P&L due to volatility of losses.

From an industry perspective, there are a broad range of industries interested in captives because it as a viable solution for any kind of industry. The main industries using captives at the moment include: retail, energy, manufacturing, financial institutions, transportation, mining, and food and beverage.

> “Latam has been experiencing important growth in the middle class over the past years, which has had a positive impact on the dynamics of regional economies and created positive financial results for some companies”

CR: Are the traditional captive domiciles (Bermuda & Cayman) still dominant, or are there emerging alternatives?

ME: For Latam captives, Bermuda continues to be the dominant domicile because of its tradition, experience and regulation. Bermuda, as well as other domiciles, has made an important effort to negotiate tax information exchange agreements (TIEAs) with many Latam countries.

Other domiciles such as Cayman, the Bahamas, Barbados, Puerto Rico, Switzerland, Luxembourg and Singapore are also options that Latam clients are willing to consider, depending on the geographies where they currently have operations and their global shareholder structure.

> “Recent tensions between the governments of both countries has put a hold on Panama as a domicile option for Columbian clients”

Regarding Panama, which is a domicile many companies – especially from Colombia – like to consider as an option, recent tensions between the governments of both countries has put a hold on Panama as a domicile option for Columbian clients. This will likely continue until the governments complete negotiations regarding Panama’s inclusion on the black list of territories.

CR: How receptive is the regulatory environment in Latam?

ME: In some Latam countries the regulatory environment is undergoing real changes. These changes are mainly focused on tax regulations, but in Ecuador, for example, there are also important alterations for the insurance sector. This creates a lot of uncertainty to decision-making, especially for offshore companies; it is not always clear which tax rules will be applied. Chile, and the recent changes in Colombia, are good examples of this regulatory uncertainty.

Latam governments are more active than ever in reviewing the white/blacklist territories and incorporating new tax rules, which are the reason the main Latam captive domiciles continue to encourage TIEAs negotiations with different countries. These talks have been very helpful for the captive industry.

Regarding insurance regulations, there are obvious differences between countries. Regulations in Brazil, Venezuela, and Argentina are more complicated. Additionally, Ecuador recently introduced a new regulation regarding the risk retention levels for the local insurance companies and new tax implications for premiums ceded outside the country.

CR: What unique challenges does operating in Latin America bring?

ME: The main challenges we face in Latam for the captive industry are:

- Educational process: shareholders and managers must be educated around the captive concept and the benefits of captives.
- ‘Short-term’ mentality: a captive solution is a long-term approach and Latam culture has traditionally had a more ‘short-term’ driven mentality. This is evolving, but will take time to change completely.
- Double fronting: Because of regulations in most Latam countries, companies require double fronting, which leads to higher costs.
- Regulatory changes and restrictive regulation as explained above.
- TIEAs: some are already in place and some are in process, but they still are not all effective.

CR: What are Marsh’s ambitions for the future in this area?

ME: Marsh visualises Latam as a growth area for captives. As the world’s largest captive manager, our goal in Latam is to continue to bring captive solutions to our clients and, over the next few years, to increase Latam captives to represent at least 5% of the total global captive count.

CURRENT CAPTIVE TRENDS IN LATIN AMERICA

Companies from Latin countries without captive traditions, like Chile and Peru, are now planning to enter the space, according to new research. These new entrants together with Brazil and Mexico (first wave) and Colombia (second wave) are creating the third wave of captives in Latin America

Written by
Javier Mirabal

Javier Mirabal, Ing, ARM, AIRM, RF is president of Mirabal Risk Management, LLC. and executive director of Fundalarys (Latin America Risk Management Association). He is based in Plano, Texas, US.

Latin America

Latin America represents 7.5% of the worldwide GPD with Brazil (39% of the GDP) and Mexico (22% of the GDP) leading the economy of the region. The other five countries (Argentina, Venezuela, Colombia, Chile and Peru) represent 30% of the economy in Latin America and together with Brazil and Mexico represent 91% of the economy. Latin America represents 8.25% of the worldwide population with Brazil and Mexico representing 34% and 21% of the total population respectively. (*Fig I: Latin America: GDP per Country (2013), Fig II: Latin America: Population per country (2013) The Latin America insurance market*).

For, the seven countries in the tables, the total insurance premium ($163.97bn in 2013) represents 3.53% of the total insurance premium worldwide (base: $4,641bn insurance premium worldwide in 2013 – Source: Swiss Re). For these countries the personal insurance lines represent 51.52% and the property & casualty (P&C) insurance lines represent 48.48%, in 2013.

For the P&C premium, auto insurance (and auto liability) represent 48.74% ($38.74bn) and the rest ($40.75bn) represents 51.26%. Also, the P&C premium without auto insurance (and auto liability) represents 25% of the total premium in the seven named countries.

From the P&C insurance premium perspective (without auto insurance and auto liability), Brazil leads with 37% followed by Mexico (23%), Argentina (17%), Colombia (9%), Chile (6%), Venezuela (5%) and Peru (3%). (*Fig 3: Latin America – Insurance premium per country in 2013 ($m)*).

The insurance penetration rate in these countries in 2013 was (overall) 3.03% of the GDP. Penetration rate only for P&C insurance (without auto insurance and auto liability) was 0.75%. (*Fig 4: Latin America-GDP vs. Insurance premium per country (2013)*).

The strength of the Latin companies

In 2013, 336 companies in Latin America (Latin companies only, excluding multinationals with operations in the region) showed sales over $1.25bn. (*Fig 5: Number of companies over $1.25bn of sales per country (2013)*).

In addition, 97 Latin companies have been nominated as multi-Latinas (Latin companies with regional operations inside and/or outside the region). (*Fig 6: Number of multi-Latinas Companies per country (ranking 2014)*.

DATA | FIG 1

GDP worldwide (2013): US$75.79trn
GDP Latin America (2013): US$5.657trn (7.50%)

Brazil (2013): US$2.246trn (39%)
Mexico (2013): US$1.261trn (22%)
61%

Argentina (2013): US$609.9bn (10%)
Venezuela (2013): US$438.3bn (7%)
Colombia (2013): US$378.4bn (6%)
Chile (2013): US$277.2bn (4%)
Peru (2013): US$202.3bn (3%)
30%

91%

Source: World Bank

DATA | FIG 2

Population worldwide (2013): 7,124 million
Population Latin America (2013): 588 million (8.25%)

Brazil (2013): 200.40 million (34%)
Mexico (2013): 122.30 million (21%)
Colombia (2013): 48.32 million (8%)
Argentina (2013): 41.45 million (7%)
Peru (2013): 30.38 million (5%)
Venezuela (2013): 30.41 million (5%)
Chile (2013): 17.62 million (3%)

55%
28%
83%

DATA | FIG 3

Country	Total Premiums	Premiums (Life)	Premiums (P & C)	Premiums (P&C) w/o auto insurance
Brazil [2]	83,810	47,830.00	35,980.00	15,000
México[1]	26,671	12,156	14,515	9,500
Argentina [1]	14,958	2,972	11,986	6,800
Colombia [1]	10,700	6,051	4,649	3,500
Chile [3]	11.1	7,415	3,685	2,600
Venezuela [4]	13,484	6,555	6,929	2,100
Perú [1]	3,244	1,497	1,747	1,250
Total	**$163,967**	**$84,476**	**$79,491**	**$40,750**

25% (24.85%)
50% (51.26%)

1. Source: Asociación de Supervisores de Seguros de América Latina "ASSAL"
2. Source: Business Insurance (consultancy firm Siscorp)
3. Source: Federación Interamericana de Empresas de Seguros "FIDES"
4. Source: Superintendencia de la Actividad Aseguradora "SUDEASEG" – Venezuela
5. Ratio: "Premium (P&C) vs. Premium (P&C) w/o auto insurance" similar year 2012 (data 2012 – Source: Asociación de Supervisores de Seguros de América Latina "ASSAL")

DATA | FIG 5

Country	GDP (1)	% (2)	Total Premiums (3)	% 3÷1 (4)	Premiums (P&C) w/o"auto insurance" (5)	% 5÷1 (6)
Brazil	US$ 2.246 tn	42%	83,810m	3.73%	15,000m	0.67%
México	US$ 1.261 tn	23%	26,671m	2.12%	9,500m	0.75%
Argentina	US$ 609.9 bn	11%	14,958m	2.45%	6,800m	1.11%
Colombia	US$ 378.4 bn	7%	10,700m	2.83%	3,500m	0.92%
Chile	US$ 277.2 bn	5%	11.100m	4.00%	2,600m	0.94%
Venezuela	US$ 438.3 bn	8%	13,484m	3.08%	2,100m	0.48%
Perú	US$ 202.3 bn	4%	3,244m	1.60%	1,250m	0.62%
Total	**US$5.413trn**	**100%**	**US$163,967m**	**3.03%**	**US$40,750m**	**0.75%**

DATA | FIG 4

Country	Premiums (P&C) w/o "auto insurance"	%
Brazil	15,000	37%
México	9,500	23%
Argentina	6,800	17%
Colombia	3,500	9%
Chile	2,600	6%
Venezuela	2,100	5%
Perú	1,250	3%
Total	**$40,750**	**100%**

DATA | FIG 6

Country	# Companies sales >US$ 1.25 billion -2013	%
Brazil	148	44.00%
México	75	22.50%
Argentina	19	5.50%
Colombia	20	6.00%
Chile	49	14.50%
Venezuela	2	0.50%
Perú	23	7.00%
Total	**336**	**100%**

DATA | FIG 7

Country	# Multi-Latinas	%
Brazil	34	35.00%
México	26	27.00%
Argentina	5	5.00%
Colombia	10	10.00%
Chile	17	18.00%
Venezuela	1	1.00%
Perú	4	4.00%
Total	**97**	**100%**

Source: América Economía

DATA | FIG 8

Ranking (premiums)	Country	Premiums (P&C) w/o auto insurance	# Companies sales >$1.25bn In 2013	Ranking (Sales)
1	Brazil	15,000 million	148	1
2	México	9,500 million	75	2
3	Argentina	6,800 million	19	6
4	Colombia	3,500 million	20	5
5	Chile	2,600 million	49	3
6	Venezuela	2,100 million	2	7
7	Perú	1,250 million	23	4
Total		**$40,750m**	**336**	

DATA | FIG 9

Country	# Companies sales >US$1.25bn-2013
Brazil	148
México	75
Chile	49
Perú	23
Colombia	20
Argentina	19
Venezuela	2
Total	**336**

DATA | FIG 10

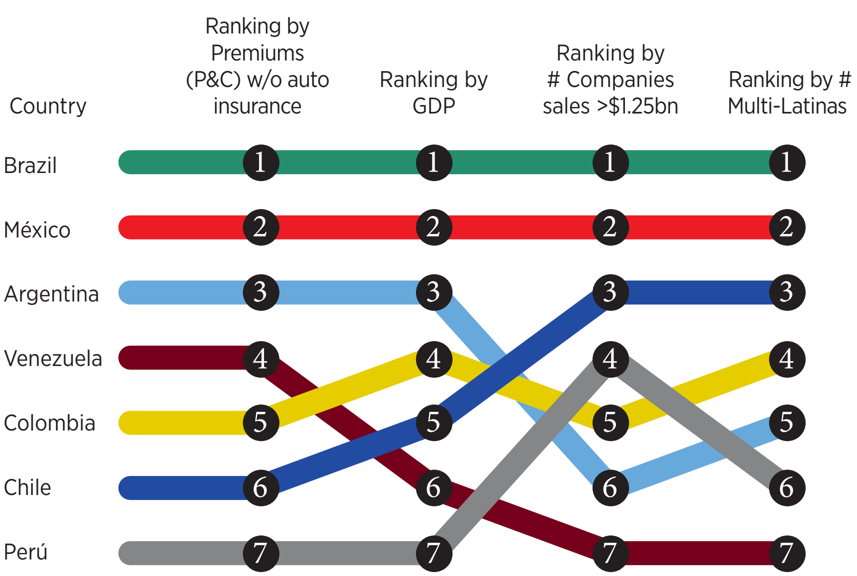

Figure 10 (*above*) shows the countries' comparison using different rankings: GDP, P&C Insurance premium (without auto insurance and auto liability), number of Latin companies with sales over $1.25bn and number of multi-Latinas. *Fig 7: Latin America: Countries Comparison of different ranking).*

According the rankings, the figures suggest:

- Brazil and Mexico maintain the consistency being first and second in all the rankings

- Argentina is third by GDP and P&C insurance premium (without auto insurance and auto liability) but is sixth in number of Latin companies with sales over $1.25bn and fifth in number of multi-Latinas.

- Colombia is fifth by GDP and fourth by P&C insurance premium (without auto insurance and auto liability) and maintains this ranking being fifth by number of Latin companies with sales over $1.25bn and fourth in number of multi-Latinas

- Chile is sixth by GDP and fifth by P&C insurance premium (without auto insurance and auto liability) but is third in both number of Latin companies with sales over $1.25bn and number of multi-Latinas

- Venezuela is fourth by GDP but is sixth by P&C insurance premium (without auto insurance and auto liability), and seventh in both number of Latin companies with sales over $1.25bn and number of multi-Latinas

- Peru is seventh by both GDP and P&C insurance premium (without auto insurance and auto liability), but is fourth by number of Latin companies with sales over $1.25bn and sixth by number of multi-Latinas.

The appetite of Latin America companies for captives

The first wave of Latin firms incorporating captives in their risk financing processes started in the early 90s led by state-owned oil & gas companies PEMEX (Mexico), PDSVA (Venezuela) and PETROBRAS (Brazil). Other Latin companies mainly from Mexico and Brazil opened their own captives at this time.

The second wave started in 2006, led by state-owned oil & gas company Ecopetrol (Colombia). Currently, 75 captives (single parent) have been incorporated in different domiciles (*source: Fundalarys*), but are they enough?

According to the volume of sales, 336 companies in Latin America (Latin companies only – excluding multinationals with operations in the region) show sales over $1.25bn, which is a good reference for companies that require a captive but only 75 of them have a captive. In this case the region has a lack of at least of 260 captives (single parent).

Conclusion: the third wave of captives in Latin America

In order to close the gap (336 Latin companies with sales over $1.25bn vs only 75 Latin companies with captives), Latin companies from emerging economies in the region such as Chile and Peru, together with companies from Mexico and Brazil (first wave) and Colombia (second wave) are leading feasibility studies evaluating to include a captive in their risk financing processes, but what will be the result of this third wave?

CAPTIVE SOLUTIONS SHOW RAPID GROWTH IN LATAM

Tom Kelly, managing director of KPMG Bermuda, discusses the expansion of the captive market in Latin America and the role Bermuda has to play in its future

Captive Review (CR): Which insurance sectors is KPMG Bermuda finding most active in Latin America?

Tom Kelly (TK): The construction, oil & gas and mining industries were among the first entities in Latam to show an interest in forming captives in Bermuda. This has remained a consistent trend with the new formations.

In more recent times however we have also seen transportation and financial services businesses also entering the captive space.

CR: Why are more and more businesses in various Latam industries now looking at captive options?

TK: There are a number of reasons. Primarily this is the result of a number of well-established and reputable entities that initially formed captives from Latam now clearly benefiting from this venture. Word has spread through various networks which has led to other risk managers and CFOs looking into the benefits of captives. After performing their due diligence more and more companies are coming the conclusion that a captive makes sense.

Written by
Tom Kelly

Tom Kelly is a managing director in KPMG's Bermuda insurance practice providing audit and advisory services to a wide variety of insurers and reinsurers including SEC registrants, large non-public entities and captive insurance entities. Kelly has been heavily involved in strengthening the relationship between Bermuda and the Latin American market by attending conferences and working with stakeholders to enhance the captive product line..

Additionally, there are now more service providers such as insurance/reinsurance brokers in Latin America that are becoming more familiar with captive solutions, which is adding to the growing captive network. In order for brokers to be competitive with each other, they need to be bringing the latest thinking on risk solutions which helps to propel the discussion around captives.

So you have the tangible evidence of long-standing Latam companies enjoying the benefits of existing captives coupled with more people, primarily brokers, pushing the captive agenda in new areas.

There are also entities, like the Bermuda Development Authority (BDA), which are participating in risk manager meetings and speaking positively about captives, which adds to the general education of Latam business owners about the captive solution.

Lastly, and sometimes most importantly, you have a number of tax information exchange agreements (TIEAs) that have been put in place over a number of years that have allowed various countries within Latam to interact with Bermuda without suffering any negative financial implications.

CR: Which Latam country initially show the most interest in developing a captive industry?

TK: Colombia became very active in the captive space four years ago. There were a lot of inquiries about captives from Colombian companies and several brokers were also pushing the concept there.

This resulted in some good traction including some multinationals which incorporated some of their business in other Latam countries into their captive structures. So it slowly spilled out of Colombia and into the rest of Latin America.

Today in Bermuda we have captives from Mexico, Columbia, Peru and Bolivia, and we expect several to come from Chile in the near future. Captive insurance solutions now seem to be spreading through Latin America quite quickly.

CR: Do you think this rapid rate of growth in the Latam captive industry is sustainable?

TK: We definitely haven't reached the tipping point yet, with regards to captives. There is quite a way to go and a significant number of profitable lines and compulsory insurance that business owners can self-insure. There are many large corporations in Latin America with plenty of potential to utilise the captive solution.

However, the significant difference between Latam and, say, the USA, is that you have quite a number of countries with specific insurance and tax laws. This is the main issue that is slowing the expansion process down the most.

I would also note that there is a level of cautiousness in the process from the Latam corporation viewpoint. The vetting process can take quite a while, and go through a significant amount of approvals. That being said, as the number of captives grow, the time between thinking about forming a captive and actually having one up and running should shrink significantly.

CR: Which countries are proving the most difficult to navigate these regulatory hurdles? Which are the most developed?

TK: Most people would probably point to Brazil and Argentina as the more difficult places to establish a captive from. In contrast, Colombia, partly due to its TIEA arrangements with Bermuda, is running smoothly. Mexico also has no real barriers for Bermuda-based captives, although the rate of captive formation is slow.

> "The captive solution has been very successful… The Bermuda experience has been noted among the current Latam captive owners"

CR: How did this close Bermuda–Latam relationship first develop?

TK: One of the key aspects is that the Bermuda Government established TIEAs with most of the Latin American countries. While a TIEA isn't a double-taxation arrangement it does allow for tax information exchange which provides a level of transparency to activities in Bermuda. The placement of these TIEAs has helped keep Bermuda off certain 'blacklists' maintained by many of the Latam countries.

On the back of these TIEAs, service providers are able to recommend a domicile, such as Bermuda, to their clients knowing that it is beneficial from a tax perspective and the nature of their insurance programmes means that self-insurance is an attractive option.

Today, Bermuda is the leading captive domicile for Latin America. We have developed a strong reputation there and the BDA has invested time and money building upon it.

CR: From a KMPG perspective, how do the requirements of your Latam clients differ from North American clients?

TK: They are actually very similar, just about 20 years behind on the growth curve. Property and casualty insurance, for example, certainly doesn't have the penetration in Latam that it does in the US, but as these markets emerge we expect insurance demand to grow with it.

I expect the demand for captives in Latin America to continue to grow and to some extent replicate what we have seen coming from the US over the last 20 years. The captive solution have been very successful for quite a number of captive owners. The Bermuda experience has also been noted among the current Latam captive owners. They enjoy doing business here and have no problem recommending Bermuda.

CR: Are you expecting to be able to apply the strategies previously used in the US in Latam in the coming years?

TK: Absolutely. There are differences in local laws that must be considered but ultimately corporations are facing the same risk as their counterparts in the US. Lines of business such as financial guarantee, surety, property and auto physical damage are fairly common areas. I would not be surprised if we see more interest in cyber risk and other risks that are currently hard to place making their way into Latam captives. The significant exceptions at the moment are in the area of medical malpractice and workers compensation, which are definitely not high on the Latam agenda as in the US.

CR: Are there any lines of business you are expecting to expand in the future?

TK: Anywhere which has compulsory insurance, such as requiring surety for projects, will continue to expand, as will other areas of property coverage. As I mentioned workers' compensation hasn't taken off in any shape or form so I wouldn't be surprised if there are legislative changes soon in Latam countries to require some form of workers' comp.

CR: Political risk has been a global hot topic at the moment in the insurance world. Do you see this line of insurance expanding or decreasing in Latam, and is a captive solution viable for it?

TK: I do not think political risk is very high on the Latam agenda from a captive view point. I think trade credit and other lines relating to the exporting of goods and services being more relevant. That being said you are beginning to see some unique risks finding their way into captives.

CR: What unique challenges does operating in Latin America pose?

TK: I do not think we have come across any real unique challenges in operating in Latin America. If anything I have found a lot of misconceptions. Overall it has been a very exciting and interesting endeavour.

The people we interact with are very professional, friendly, and respectful of our time and effort. They also know their business very well. For the most part we are explaining how Bermuda works and the types of risks that we see in Bermuda. We definitely have challenged them to think about broadening how they think about risk and how captive insurance can be a solution, not just an expense.

CAYMAN CONTINUES TO WOO LATAM CAPTIVE OWNERS

JS de Jager of CSI International Underwriting (Cayman) Ltd explains how Cayman's captive industry has evolved in recent years and where it is headed in the future

Written by
JS de Jager

JS de Jager joined CSI International Underwriting (Cayman) Ltd in 2007 and is directly responsible for the oversight and management of an extensive portfolio of captive insurance companies, investment companies and financial management companies. De Jager holds a range of directorships, including funds and investment management companies.

Captive Review (CR): How has Cayman developed as a jurisdiction over the last year?

JS de Jager (JJ): The last year proved to be another busy year for Cayman. Its position as a jurisdiction of choice for captive insurance companies is growing from strength to strength each year and 2014 was no exception. After ongoing consultation between the regulator and the captive insurance industry, the Cayman Islands insurance (portfolio insurance companies) (PIC) regulations passed on 16 January 2015, along with related sections of the Insurance (Amendment) Law 2013. The PIC legislation and accompanying regulations reinforces Cayman's leading position over other jurisdictions in terms of sensible and proportionate regulation, innovative legislation (based upon a trustworthy and reliable legal system) and the high level of governance and compliance afforded to it. Cayman enjoyed more steady growth, with 22 new captive insurance companies formed during 2014. This increase is evidence of the ongoing and ever increasing strength of Cayman in the industry. The further signing of more tax information exchange agreements during the year also again confirmed and highlighted Cayman's continued efforts to stay ahead of the game when it comes to complying with international standards for transparency and regulation.

CR: How has Cayman's position as a key Latam captive jurisdiction evolved?

JJ: Cayman currently has bilateral tax information exchange agreements (TIEAs) with the following Central and South American countries: Argentina, Brazil, Chile, Colombia and Mexico. That already puts Cayman in good stead with the biggest markets in the region and discussions are ongoing to increase that number to further strengthen Cayman's position in Latin America. With a lot of focus being put on business development in the region, Cayman is becoming increasingly visible and big business in the region is catching on to that. More and more enquiries are being received from Latin American businesses regarding the structuring of captive insurance companies and other entities that will enhance their company's growth potential internationally and in their local markets. Cayman's highly regarded risk-based captive insurance regulation and legislation is a very attractive model for companies in the up and coming Latin American markets.

"More and more enquiries are being received from Latin American businesses regarding the structuring of captive insurance companies"

CR: What sets CSI apart from its competitors in Cayman and in other jurisdictions?

JJ: As an independent and innovative company, CSI International Underwriting (Cayman) Ltd is a representative of Cayman's particular developmental path. Clients appreciate the personal and business relationship that can generally only be delivered by smaller organisations. A large network of accessible professionals enables the independent to provide products and services that can be custom-made to meet the clients' particular needs.

At CSI we don't market ourselves as experts in the direct negotiation of reinsurance treaties but rather, we work hand-in-hand with external professionals that achieve our clients' and potential clients' goals. The same applies to underwriting issues and claims handling – we work with external, professional service providers through our own or our clients' network of industry contacts. You don't need to be big or connected through a network of large offices to provide a complete service. Working with external service providers enables us to deliver a comprehensive package to the client, while concentrating on the specific requirements.

At CSI we treat our clients as individuals with unique and uncorrelated needs and will always strive to achieve what is best for them. As an independent manager within Cayman, CSI can deliver an alternative risk programme to a client that specifically meets their requirements. There are no restrictions on the variety or scope of the insurance sector that can be covered with the close network of specialists in the various fields available to us.

CR: What are your predictions for Cayman's regulatory environment over the coming year?

JJ: The PIC legislation and accompanying regulations that were passed in 2015 both exemplify and reinforce Cayman's leading position over other jurisdictions in terms of sensible regulation, innovative legislation based upon a reliable legal system and the high level of governance and compliance afforded to it. The PIC legislation is considered more robust than the incorporated cell company (ICC). During 2015 the local industry will keep working to promote the services that are valued so highly by our clients and envied by many other jurisdictions.

We should expect constant review of regulations, but would expect that the key regulatory developments in this coming year will be more in the line of the further introduction of clear policy statements to enhance Cayman's reputation as the captive insurance jurisdiction of choice. The financial sector in Cayman is working closely with the Ministry of Finance at all times to ensure Cayman stay on top of new trends in the insurance market. In the broader insurance market Cayman is also growing in the reinsurance sector and we expect the regulator to also focus on that area to streamline and get the regulations in place and enhance the attractiveness of the jurisdiction for reinsurers.

With regard to the insurance sector, the updating and issuing of these policy statements and regulations have and will be considered a positive step forward, generally formalising what has always been accepted as informal practice throughout the industry. The Cayman Islands remains the leading jurisdiction for healthcare captives, with 34% of the captives in this classification. However, Cayman captives are increasingly being used for more innovative uses, such as insuring against cyber risk, terrorism threats and environmental pollution.

"The financial sector in Cayman is working closely with the Ministry of Finance at all times to ensure Cayman stay on top of new trends in the insurance market"

CR: Are there any specific challenges CSI is predicting to face?

JJ: Like most other insurance managers in Cayman there will also be an ongoing challenge to reinforce and highlight Cayman as the domicile of choice. Increasing competition from now more than 80 captive domiciles worldwide will require increasing diligence on behalf of not only CSI but the whole Cayman industry to continue to attract new captives. We believe that in a marketplace that is becoming increasingly merger-led, CSI's independence stands out as very beneficial. As in many financial areas, consolidation seems to be a major theme and it is inevitable that further consolidation will take place. Constant acquisition will mean that larger offices will continue to hold a large market share of the business. Learning to compete with this will certainly be a challenge for CSI. That said, it is a hallmark of CSI that we are able to operate to our own high standards and will continue to strive to achieve what is best for our current and future clients.

THE BRITISH VIRGIN ISLANDS: OPEN FOR BUSINESS

BVI Finance and Kay Reddy of Blenheim BVI discuss the benefits for Latin American businesses to domicile captives in the British Virgin Islands

Captive Review (CR): How did the British Virgin Islands first develop as a captive jurisdiction specifically for Latin American businesses?

BVI Finance: The British Virgin Islands (BVI) is a modern, forward-looking international financial centre with high-quality services that are internationally recognised and well regulated. We are the premier corporate domicile where approximately 500,000 active business companies reside. The domicile offers a portfolio of products and services in trust and estate planning, funds and investment business, captive insurance, ship and aircraft registration services; as well as advisement and support services from some of the world's leading trust companies, law firms and accounting firms all of which reside in the BVI.

Following the success of the BVI's International Business Companies Act, it became apparent that newly registered companies, across a number of different sectors, needed additional services and the BVI positioned itself to offer captive services in 1990. Since then, the BVI has gained recognition as the domicile of choice for captives of varying capacities and the BVI's captive services sector has grown and diversified. The flexibility of our offer is attractive to North America and now increasingly relevant and attractive to the Latin American (Latam) market.

As a financial centre, the BVI started to grow strongly in the 1980s after we introduced the BVI Business Companies Act. At the same time, Panama was experiencing a period of reform which led to many Panamanian law firms and trust companies establishing a presence in the BVI. This was instrumental in the BVI becoming a major financial centre.

Written by
Kay Reddy

Kay Reddy has been the director of the Blenheim Group for over a decade. Kay has been involved in the development of the Blenheim Group and specialises in the mutual fund and captive insurance sectors. Prior to this she was director of Barclays Private Banking in the British Virgin Islands and manager of the International Trust Group of Companies. Kay holds a B.Sc. in Mathematics, Operations Research, Statistics and Economics from Warwick University.

Now, the BVI Business Company has led the BVI to become the biggest company formation centre in the world, our portfolio of trust companies shows our significant Latam connection.

CR: What makes the BVI attractive for captives?

Kay Reddy (KR): The BVI's effective and flexible Business Platform is used and recognised by captives across the world. You can hold any number of shares or companies with no-par value stock. We even have the capability to support segregated portfolio companies, which has become very popular for captive insurance companies as it allows them to separate uncorrelated risks into individual portfolios.

BVI Finance: The BVI is committed to offering the very best service structure and constantly looks to differentiate itself in the market. Recent changes to the legislative regime have given us yet another edge in that direction. BVI Business companies are widely used in multinational cross-border transactions; this has strengthened the jurisdiction's profile and helped to maintain our track record of being internationally compliant and transparent to attract best-in-class businesses and services to meet our client's expectations.

CR: What is the BVI's relationship like with the Latam industries?

BVI Finance: In April 2002, the BVI made a commitment to work with the OECD to develop principles of transparency and exchange of information in tax matters. There are currently mutual agreements in effect with Argentina, Columbia, Chile, Mexico, Belize, Costa Rica and we have been listed as compliant with 27 tax information exchange agreements (TIEAs).

The BVI is widely used in Latin America for corporate structures in wealth planning and investments. We have built a close relationship with the professional service firms who offer BVI products to their clients and have committed to closer ties with the introduction of TEAM BVI - industry ambassadors- who will advocate and assist where necessary on behalf of the jurisdiction.

Our relationship with Latam has developed and evolved since we began working together in the 1980s. The captives industry in Latam is still relatively new and has allowed the BVI to work with the industry from its beginning.

KR: Understanding the local language and culture is extremely important to us, which is why we have developed a strong network of offices and local representatives in Latin America, who work directly with our clients in helping them fulfil their requirements.

CR: Are language barriers a significant hurdle to securing business in Latam?

KR: A lot of Latam stakeholders are thankfully bilingual, therefore having company documents in English does not pose any significant problems.

On the other hand, captives and mutual funds have been a little slow to develop as a result of language barriers, as we need to deal with policy documents and actuarial reviews, which involve relationships with a wider range of professionals.

BVI Finance: The BVI has developed a strong relationship with the private sector in varying jurisdictions. Consequently, we are able to confidently support any business ventures that may develop in the region. We have developed strategies for engaging TEAM BVI in all our major jurisdictions; ensuring the BVI is able to meet the needs of our clientele in the Latam region, efficiently.

CR: Has BVI Finance been targeting specific countries within Latam to market the BVI as the captive domicile of choice?

BVI Finance: As previously mentioned, we have a very strong link in Panama and BVI Finance has also been targeting Colombia, where several of our colleagues have secured strong business leads. Colombia has changed a lot and is in itself emerging as a recognised financial centre.

As a jurisdiction, our strategy specifically includes building our relations with Columbia, Argentina and Peru for new and introduced business for financial services and investments.

CR: Given the small size of the current market in Latam is there competition between local offshore domiciles for Latam's business?

KR: BVI has a head-start because of our relationship with the corporate and trust industry, where other jurisdictions are not as established. However, we won't be complacent because the other domiciles certainly offer a good product and there is competition.

What we have seen is that the other local offshore jurisdictions have become product specific to a degree. The BVI targets the generic industry captives such as industrial businesses, large groups or multinationals. Bermuda, on the other hand, is handling multi-billion dollar captives which we are not competing for as they are too large for our service providers. Cayman has become popular for health in the captive industry and a number of jurisdictions, like Anguilla, are targeting single-parent and group captives.

There is competition but the jurisdictions tend to stick to their niches. Ultimately, it is a small market but there is plenty of business for everybody.

CR: What sets the BVI apart from its competitors in this regard?

BVI Finance: We offer a complete service landscape as all the major law and accountancy firms are here as well as insurance managers, so we can provide a full service. Telecommunications is vital to the BVI so our infrastructure is very solid for communication and access.

CR: What is the private business relationship like with BVI regulators?

BVI Finance: Historically, there has always been a close relationship between the government and the private sector. The first insurance law was introduced in 1994 and was then reformed in 2008 with a new act. We have also carried out a consultation with the sector recently as the government is looking to update the legislation again. This will introduce a new class of captive services to address the increase in group and single-parent captives here. It will also help our US-facing businesses with tax requirements and segregated portfolios as they are becoming increasingly popular. This close relationship means the law can be revised on a fairly regular basis to keep abreast of current developments and requirements.

CR: What would you say is currently the biggest hurdle to Latam's captive industry expansion? Is it being tackled?

KR: Ultimately, it's just new. Most of Latin America is based on Civil Law as opposed to the UK and European style. It's primarily a matter of marketing and educating people to make sure they understand what captive solutions can offer. People will not spend the large sums needed to set up a captive if they aren't comfortable with the concept. However, as understanding develops more, you will see the benefits of the industry.

The other hurdle, again related to the market's development, is the current appetite for captives in Latam. In Europe and the US, the captive markets were originally driven by the hardening insurance markets; as premiums grew, people began to invest in alternative insurance solutions such as captives. In Latin America at the moment, the insurance industry is providing relatively competitive premiums meaning there isn't a great need for captives.

CR: What is BVI's Latam strategy going forward in 2015?

BVI Finance: We see Latam as a new and vibrant market with lots of growth potential. Our strategy involves spreading information about the BVI throughout Latin America. We are really at the first stage of explaining who we are and what we do. Financial services often requires long lead time, and so the conversations we are having now could take three to five years to progress. We don't expect the Latam insurance industry to grow rapidly overnight but over the next few years, we hope to see steady expansion.

The BVI is very confident with our newly enhanced legislation for captive companies and we are certain that it will benefit the Latam market. Our portfolio of products and services for wealth management structures and investments also present an attractive platform, positioning us as the one-stop-shop for the Latam market.

> **"There is competition but the jurisdictions tend to stick to their niches. Ultimately, it is a small market but there is plenty of business for everybody"**

CR: How confident are you that Latam's captive industry will continue to grow throughout 2015?

KR: Latam falls behind in the development of captives compared to the more established US and UK markets, but if it continues to progress at its current rate, the use of captive-like products will certainly grow.

We are aware that this is a fairly new concept for the Latam market and the BVI is well-positioned to benefit from its growth and development in this area.

CAYMAN – WELCOMING LATAM CAPTIVES

Adrian Lynch of IMAC speaks to *Captive Review* about Cayman's burgeoning captive industry

As Latin American countries continue to see improving economic returns (Brazil and Mexico, for example are both on the top 10 list of global economies), the corporate appetite for captive insurance companies is keening as companies are looking for all of the risk transfer and other benefits that such an arrangement can provide. The insurance market overall is maturing in the region as corporates grasp a greater understanding of captives, and the regulatory frameworks within which they operate undergo steady, progressive modernisation.

The Cayman Islands, a jurisdiction with a 40-year track record of providing exceptional products and service to the captive insurance industry, is ideally placed to be the default domicile for Latin American captives. Throughout that history, some of the world's largest companies across a wide range of industries have entrusted their captives here. Latin American families have long used the Cayman Islands to facilitate generational and tax planning through the use of foundations and trusts.

Relevance for captives

In order to understand the Latin American market, one must understand that societally, it is highly patriarchal and this same hierarchy carries into the commercial infrastructure of many businesses in Latam. Many successful businesses are privately owned and though one might want to talk about captives, one must also be willing and able to discuss the infrastructure within which the captive will sit. This will require involved and informed tax and legal planning, again outside the scope of any captive manager, but highly material in terms of developing a captive as a long-term strategic play for any Latam business. Aon manages a number of private placement life insurance companies (PLI) that also have a role to play in future structural Latam work to include captives.

Written by
Adrian Lynch

Adrian Lynch became managing director of Aon Insurance Managers (Cayman) Ltd. in March, 2014. Prior to this, Lynch spent seven years as the CEO of a private client advisory group, offering Private Placement Life Insurance structures. He will also serve as managing director of Aon Risk Solutions (Cayman) Ltd., Aon's broking operation in the Cayman Islands.

These are two interesting and intersecting points – an increase in the interest and appetite from Latin American companies for captives and Cayman's ability to provide the highest quality captive products and service providers to accommodate this burgeoning new market. However the intersection needs to be approached very carefully by all practitioners.

Captive benefits

With the heightened economic development in Latin America comes an increase in infrastructure, such as governance and transparency/compliance requirements and advanced technological innovation. This has led to a demand for more sophisticated risk management strategies, of which captives are now playing a significant part.

Companies in the region are growing at pace, branching out globally across energy, mining, manufacturing, engineering, food and beverage and entertainment industries. These 'multi-Latinas' often have specific needs that captives can effectively be used, addressing specific multi-national exposures. It is not just the large companies that are looking at captives. Small to mid-sized companies are investigating and establishing captives to support their businesses.

These companies are looking for solutions to some of the same challenges that face companies the world over, including: diversification of operations; efficiencies improvement, particularly across multinational organisations; improved risk management, including through the retention of significant elements of risk; flexibility in coverage structures; the ability to pool risks from across various business units; asset protection and perhaps to improve on tax efficiencies. Captives also provide the ability to retain earnings and make revenue on retained premiums that would have normally gone to the traditional market, as well as to provide coverage when the cost of traditional insurance is too high, because of the size or complexity of the risk.

We always recommend that those considering a captive hire an expert to conduct a feasibility study to ensure that a captive is a solid and viable option. Feasibility studies contain a direct correlation between the quality of the data feeding into them and the quality of the outcome of the study. Latams have historically been perceived as reluctant to share full data, with the result of decisions being made in a vacuum and perhaps not being in the best interests of the company long term. I emphasise again a captive is a medium-to-long term strategic investment and the challenge with Latams is that they have heretofore been unwilling to look beyond a two- to three-year horizon, particularly in a soft market.

Specific tax and legal advice are also recommended to assist with domicile selection and information on capital requirements. Tax regulations vary from country to country and could have consequences on both captive and parent. Again, though Cayman has no tax obligations it would be remiss of any manager to ignore potential tax implications for the client. The US has signed tax information exchange agreements (TIEAs) with many Latam countries and historically many Latams have run many of their structures through foundations in Panama for example. The TIEA signed between Panama and the US will be a very interesting source of data for the US. Again to labour the point as the risk management requirements of the Latam clients mature, then so should the approach to disclosures and compliance. None of my fellow captive managers will disagree that Latams have historically been fee sensitive and have high expectations as to what is provided in advance of any feasibility discussions. Cayman stands ready, willing and able, but Latams as a market must adjust their own expectations in terms of subscribing to regulations and standards that heretofore might not have been as onerous.

Cayman is politically and economically stable. As a British overseas territory, it has a democratically elected government as well as oversight by the governor, as the Queen's representative, and a legislative infrastructure that is based on English Common Law. Cayman is rated Aaa by Moody's and is on the OECD's list of approved jurisdictions, having actively participated in all international regulatory and transparency initiatives, based on a level playing field, for more than thirty years. In 2005 the International Monetary Fund (IMF) gave Cayman a nod when it stated: 'The measures and policies in place for insurance supervision are sound'.

Being an OECD 'white listed' jurisdiction means the active process of negotiating and implementing TIEAs with other countries. Currently, Cayman has such arrangements with Argentina, Brazil and Mexico, and is in current negotiations with Chile and Colombia. Colombia, in 2014, put Cayman on its own white list in acknowledgement of Cayman's significant contribution to the international regulatory and transparency process.

We can also draw some conclusions from the latest statistics from the Cayman Islands Monetary Authority. These numbers indicate that Cayman continues to maintain its position as the second largest captive insurance domicile in the world, trusted by the world's largest and most influential companies. As at 31 December 2014, the total number of captives domiciled in Cayman was 759, pure captives representing 415 of these and a further 139 being segregated portfolio companies (with some 600 cells), writing total premiums of $12bn and holding total assets of $51.5bn.

"In short, Cayman has been long operating under the philosophy of providing and attracting 'Clearly Better Business'"

All of this business is attracted to the stability and commercial ease in the Cayman Islands. The regulatory infrastructure has been established on a risk-based model that applies appropriate amounts of regulation according to the size and use of the captive. The legislation is modern and the legislators, the regulator and industry (through the Insurance Managers Association of Cayman (IMAC)) are continuously challenging each other to raise the bar as to what Cayman should be anticipating in the future regulatory environment. NAIC equivalency is something that has been raised within Cayman in order to attract reinsurers and it reflects the maturity of the jurisdiction when all parties are willing to sit and address the feasibility of the same.

Cayman's segregated portfolio company structure offers the flexibility of ring fencing assets and liabilities, providing for economies of scale and limiting potential exposure to unrelated parties. The latest piece of legislation to pass (with accompanying regulations) is that for the portfolio insurance companies (PICs) which will enable an SPC to incorporate by establishing a PIC as a separate incorporated subsidiary. This legislation is simple, yet highly effective and is being touted as being more robust that the incorporated cell company legislation offered in other jurisdictions. It is through this type of innovation that Cayman continues to capture market share, especially in the Latin American region.

In short, Cayman has been long operating under the philosophy of providing and attracting 'Clearly Better Business'. And it shows. The industry remains robust and continues to innovate, the regulatory environment remains sound and clients are continually attracted to these shores, to be served by the world class professionals that have also been attracted to the security and the high quality of the jurisdiction.

As managers I reiterate to my staff that we are all tenants in the great Cayman Islands and we have an obligation and a responsibility to hand it to the next generation of business people in better shape than we received it. Latam will be a growth market for Cayman and we all have an obligation to demand of our Latam clients a higher standard of doing business. Those Latam clients who have subscribed to that model have immediately embraced the changes and are the better for it. Exciting times for Cayman.

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The Insurance Managers Association of Cayman is a non-profit organisation run for and by Cayman's captive insurance industry, including insurance managers, Cayman captive insurance companies and service providers. The association is the unified representative of the captive industry, acting as a liaison with the Cayman Islands Government, the Cayman Islands Monetary Authority (CIMA) and the private sector, to ensure that its members' interests are represented.

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KPMG has been providing audit, tax and advisory services to the Bermuda captive market for over 50 years. Our industry experts provide insight and value through formation assistance, regulatory and tax advice, capital management, actuarial and audit services. We work closely with our clients to create opportunity and to manage risk. Our clients include US, Canadian, European and Latin American owned captives writing all lines of business.

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