Insurance and P&I

London firms embark on the Bermuda trail

Although there is strong commercial logic for setting up in the island, the potential impact on other interests must be considered, writes **David Roberts**

PLANS by Kiln plc to set up a Bermudian holding company for the Kiln Group and establish a new Bermudian insurer should soon be finalised. Bermudian firm, Validus Holdings has recently bought Talbot Holdings, a mainly Lloyd's operation.

Whether coming or going, Bermuda seems to be 'hot' for reasons not solely meteorological. Many London market insurance entities have set up business in Bermuda over the last few years. What is the attraction and what is actually involved?

Roberts: many obstacles.

The commercial logic varies, but includes:

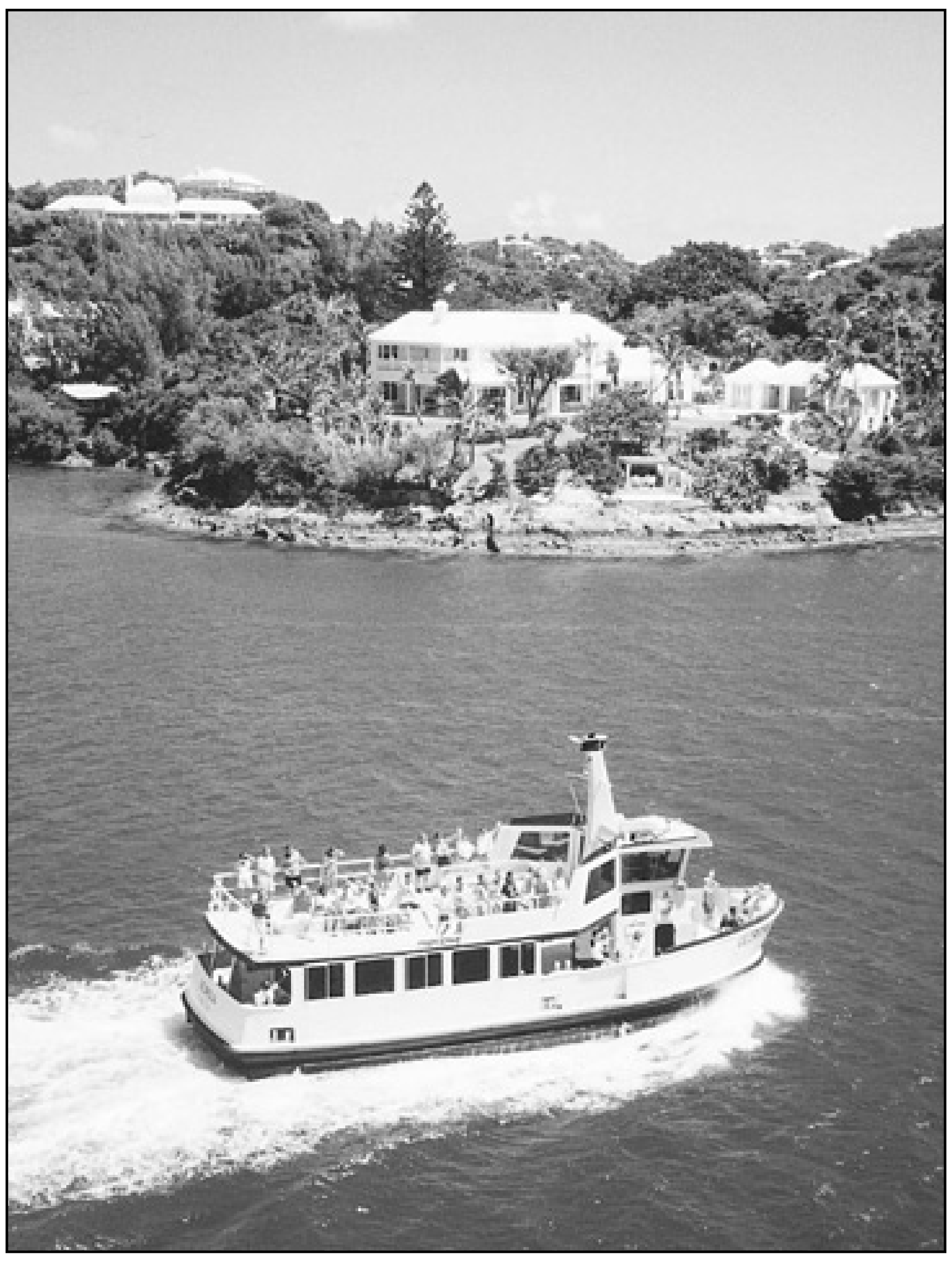
- Closeness to the US market, including the convenience of compatible time zones;
- Consistence with greater internationalisation generally;
- Sources of alternative underwriting capital are comfortable with and have experience of transactions in Bermuda;
- Many institutional investors interested in insurance businesses find Bermuda an attractive marketplace;
- Presence in important marketplaces alongside peers;
- Flexibility of running an integrated insurance business with capacity in different markets in parallel.

However, it is not all 'pros' and no 'cons'. Bermudian insurers have limited access to direct business — it is a reinsurance market. Insurance entities must also consider the effect of setting up in Bermuda on third parties.

For a Lloyd's group, it is important to assess the impact on external names. The managing agency, Lloyd's and Financial Services Authority protections will still be in place and unchanged, and the tax position will be unchanged. However, the syndicate's access to business developed by the group may be limited by the internal competition from the Bermudian insurer.

For brokers, the impact depends on the nature of the business to be underwritten in Bermuda. For some classes, like US property catastrophe business, there is such a concentration of capital already in Bermuda that the establishment of another player will only improve an established market for the brokers.

For customers, so long as their brokers have efficient access to a broad market of underwriters, the main issue is security. Insurers looking to secure business from third-party markets need to establish the capital, operational and risk management bases to secure an appropriate rating.



Bermudian insurers have limited access to direct business. Roger Paice Associates

What is involved? It is fairly straightforward process to set up either a Bermudian company or a Bermudian insurer, and this ease is a key element of the attractiveness of Bermuda.

There are regulatory hurdles to leap, but these are in the expected areas, and the provisions concerned are not onerous. Compliance with fit and proper requirements: the need for a Bermudian place of business, and the requirement for professional sign-off by firms approved by the Bermudian Monetary Authority are all as one would expect.

While being exempt from the general provisions relating to employment of minimum proportions of Bermudian residents, there are residence requirements for certain key posts.

There are no general minimum capitalisation requirements for a Bermudian company. Bermudian firms are not liable to income or capital taxes in the country. The holding company will not be subject to Bermudian insurance law — it will be able to prepare its shareholders' financial statements under whatever GAAP it wishes.

Current capital requirements and solvency margins for Bermudian insurers are not particularly onerous, although in practice an insurer wishing to write non-group business will need to have enough capital to support the required rating, and this is likely to be far in excess of its regulatory capital requirement.

The Bermudian tax regime applies to companies resident in the country. For Bermudian residence to be maintained, a company's high-level central management and control needs to actually exercised in Bermuda.

The residence tests are the same for an insurer as for a holding company. However, the breadth of the management activity concerned is almost certainly wider in the case of an insurer, as it has day-to-day operations to be managed as well as its high level direction.

This requirement clearly has a serious impact on the people in the business. Senior staff will need to be based in Bermuda for a significant part of their work.

For US and other non-UK shareholders, the position is often complex and varies greatly depending on the precise circumstances of the securities concerned and the shareholder. It is necessary to be careful in designing the arrangements concerned.

Generally, in view of Bermuda's offshore status, the benefits of tax treaties in reducing tax 'friction' for shareholders are limited.

UK income taxes will be levied on a UK corporate shareholder of the Bermudian holding company on an income arising basis if that company is assessed to be a Controlled Foreign Company under UK tax law. Equivalent legislation applies, albeit differently, in the US. Anti-avoidance provisions also exist in relation to individual UK shareholders.

So far as the creation of the new holding company is concerned, UK shareholders may be entitled to roll over relief and it is normal to apply for prior clearance in this latter regard. Stamp duty may be chargeable at 0.5% of the value of the shares issued on the exchange, although an exemption is available.

Dividends received by UK individual shareholders from Bermudian companies are taxable, currently without the benefit of the deemed tax credit which attaches to UK source dividends, although this may change as a result of the current Finance Bill.

UK corporate shareholders pay corporation tax at their full marginal rate on dividends received from Bermudian companies, although there is scope for relief in relation to underlying tax paid.

Before setting up a business in Bermuda, insurance entities must consider the impact on their business of maintaining a Bermudian structure. In particular, the effect of capital requirements should be carefully assessed, especially compared with a Lloyd's operation, and both the difficulties and the costs associated with the people issues should not be underestimated.

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A compendium of crazy incidents at Lloyd's

A CARTOON auctioned at Bonhams this week depicting supposed fisticuffs at Lloyd's reminds us that there have been, and are, flashes of humour in even the most composed business environment, *writes James Brewer.*

Veteran Lloyd's broker Antony Delderfield has been taking it upon himself to chronicle some of those moments, drawing from six decades of association with this unique market.

He has witnessed scenes to make him laugh — and cry (he lost money as a name in the underwriting crash of the 1980s) — since he first joined the market. He arrived as a youth in 1941, only to be whisked away for war service and return in 1947. He has always been a marine broker, from his early days at Wigham Richardson, has amazing knowledge of the Greek and Far East shipowning scenes, and is still going strong as a consultant to AJ Gallagher (UK).

Inevitably, Mr Delderfield derives much of the material he has mined from stories about the characters, or 'jokers', in the underwriting room. One of them as a Christmas-time wheeze stealthily attached a safety pin to the immaculate jacket of former Lloyd's chairman Sir Eustace Pulbrook after he returned to lunch.

The safety pin held a length of string pulling along the wooden duck which had been bought as a present for the underwriter's small son.

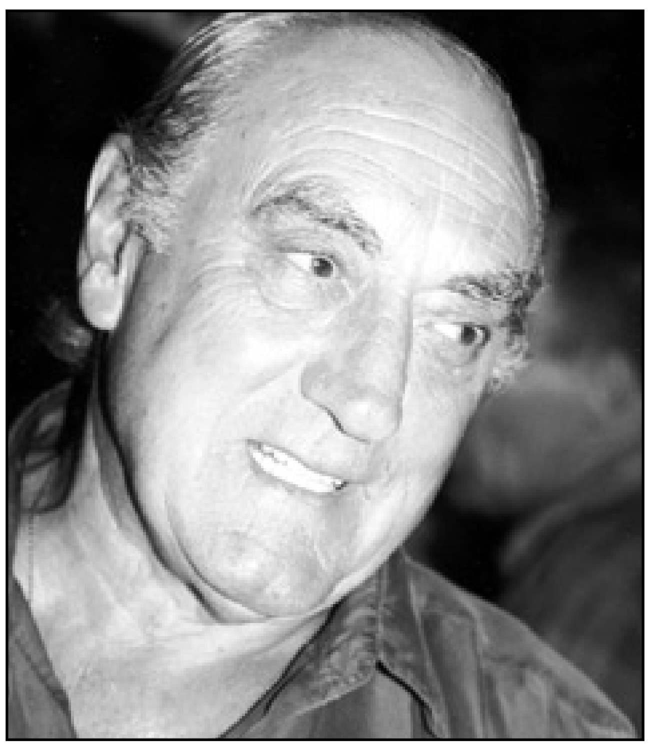
Everyone else in the room was soon chortling at the sight of the most prestigious figure at Lloyd's towing unawares a small nodding toy.

When Sir Eustace found out, he managed to keep his habitual calm, and turned to his deputy at the box saying very loudly: "Mr Barclay, please have Donald returned to Mr Disney."

Loud applause. Sir Eustace dealt with the next broker in his queue as though nothing had happened.

Mr Delderfield himself had to contend with some rum claims, such as the Indian Ocean grounding when a cargoship master reported: "We hit an island that was not there."

George Stewart, president of Stewart Smith USA, was a charmer but another practical joker, not above surreptitiously substituting a colleague's passport with a spoof document containing an 'identity photo' of child film star Shirley temple, just ahead of a business trip to Denmark.



Delderfield: witnessed scenes to make him laugh and cry.

Those were the days, when as many as 140 marine underwriters held court every day, and were asked to write all sorts of risks, and sometimes got up to all sorts of, unamusing, tricks behind the backs of the names.

In these days of contract certainty, there can seem to be less fun, but a recent speech by Simon Beale, marine underwriter for Amlin, to average adjusters, shows that he and his colleagues still need a sense of humour.

"I have to say that if you do not do fun, it is likely to be drilled into you at Lloyd's," said Mr Beale. "If you don't do fun, at least be prepared, for it happens all around us."

Mr Delderfield tapped all his shipowning, underwriting and broking contacts for his compendium of crazy incidents. Spiced with film stars, royalty and even a seductive KGB agent, his book shows that humour is the best policy.

Humour at Lloyd's, by Antony Delderfield. Copies may be purchased directly from the author at 9 Alie St, London E1 8DE, or from Heather Ewbank, Lloyd's Club, 3 Carlisle Avenue London EC3. Price £10, with all profit after publishing costs going to the Royal National Lifeboat Institution.

Gard celebrates 100 years with rating upgrade from S&P

NORWAY'S Gard is riding high this year, *writes Denzil Stuart.*

Not only is the major marine insurer celebrating its 100th anniversary, but it is cock-a-hoop about its rating upgrade from Standard & Poor's. Both the P&I club and Gard's marine and energy business are now A+. That is the highest rating of any marine mutual.

On top of this, chief executive Claes Isacson says the P&I renewal in February was one of the best seen for a number of years. The club has recorded an increase of around 15m gt, bumping up the total to an impressive 150m owned and chartered tonnage, combined with a very low turnover.

Writing in *Gard News*, Mr Isacson says the club also achieved its general increase target of 5%, which, according to Gard's financial plan, should be consistent with a long-term combined net ratio of 105%.

Final 2006 policy year results will be revealed in the next few days, and it looks certain they will be very positive.

However, all this good news is tempered by a warning from the Gard supremo not to be complacent in an uncertain world. Like many of his peers, Mr Isacson concedes it is becoming increasingly clear that casualties and liabilities will be more serious.

He says: "This year has already seen the volume of large liability claims in shipping increase sharply, and almost all the main insurers have at least one severe incident on their books."

Also: "Pool claims are running at record levels, and after 12 months the loss estimates for 2006-07 were nearly double those of 2004-05 [the worst in many years], and likely to deteriorate further."

As a result, is consolidation in the industry looming? Mr Isacson gives a clear hint that it is.

Meanwhile, as part of its centenary celebrations, later this year Gard will publish a book about its history.

Arendal, the insurer's base, was the home of several marine institutions in the early 1800s, and although the wooden fleet registered in the port inevitably declined, the town saw a succession of insurance ventures.

Owners of sailing ships, who realised they were increasingly vulnerable to liability claims, decided to band together to keep costs down, and formed Gard, from an old Norse word meaning 'one who guards'.

Gard started trading on January 1, 1908, with 148 vessels on its books, at that time roughly a fifth of the Norwegian sailing fleet.

Seacurus bridges key insurance gap

By Denzil Stuart

A NICHE gap in marine insurance cover, brought about by the boom in shipping markets, has been filled by Seacurus, the Tyneside specialist company, with the support of Lloyd's underwriters.

Seacure 60, claimed to be a world leader, is a cancellation insurance that protects shipowners from loss of revenue should a time charterer cancel due to the length of time taken to repair a damaged vessel.

As a result of bulging newbuilding orderbooks, many repair facilities are now closed to owners.

Seacurus director Thomas Brown said the policy was devised in response to the current bountiful freight markets, which have seen many vessels fixed on long-term charters at unprecedented rates of hire.

This has had a knock-on effect for busy yards, therefore increasing repair times, and the risk that charterers will cancel contracts with owners and find an alternative vessel.

The policy is designed for the larger ship market and seeks to meet the current 60 day-plus standard cancellation periods found in long-term containership charter parties aimed at vessels over 2,500 teu capacity.

However, the product does have cross-sector appeal. "This is a specialist cover that will indemnify the owner for the difference between the original time charter rates and the new market rate," Capt Brown told Lloyd's List.

Capacity limits are set for up to $25m per enquiry.

Seacurus, established in 2004 by a group of like-minded professional practitioners with seafaring, P&I, legal and insurance backgrounds, aims to provide innovative solutions to modern problems alongside a broad range of traditional services.

Its services are supported by expert input from Elias Marine Consultants in Cyprus, Gray Page, Cooper Gay and Arthur J Gallagher.

Why vision of the future is achieveable today

London insurers need to click in to up-to-the-minute claims information so that they can keep the vital reserves kitty under control, writes **Richard Garnett**

EVERY penny counts for every organisation in the London market, so in a soft market, no one wants to keep larger reserves than they absolutely have to. To keep one step ahead of the competition, it is essential to have real-time reserve information.

To some, this might seem like a vision for Lloyd's in 2020, but it is achievable now. With electronic systems, you can have a bang up-to-date view of what your claims are at any given moment at the click of a button.

It is no secret that Lloyd's and the London market are one step behind the rest of the world when it comes to using new technology. But in a market where billions of pounds are kept in reserves and millions paid out in claims every week, it is remarkable that getting the claims information from client through broker to reinsurer still takes so long.

Just last week, I spoke to one person who had a claim for £12m that took a year to get to his desk. That is a year where a company did not know about a claim for millions of pounds, or the reserve position it should have been in – just because the paperwork got stuck in someone's in-tray.

In this day and age of electronic communication there is no need for this kind of delay. Indeed, it could cost companies huge sums in interest. At a basic risk-free rate of return of say 5%, £12m would give £600,000 over a year. And while this is not an everyday claim, multiplied over many accounts, this could pay the salary of your chief financial officer — and then some.

Most major firms now have sophisticated internal computer systems that can tell their company their reserve position every week or, if need be, every day.

But what they are missing is the final link – the communications system that will allow the claims information to flow from the client to the broker and underwriter at the same time. This allows reinsurers to know about the new claim and what their new reserves position should be instantaneously.

There is an old adage — garbage in, garbage out — that applies here. If the information being inputted on claims is out of date or wrong, and this information is then being used to calculate the figures for reserves, then a company's whole position could be wrong.

If you have up-to-date claims information, you also know the terms of that policy and the amount of days you have to pay, be it 30 days, 50 days etc and put the money in a place where it is working for you. When you are getting to the point when you are talking about millions and tens of millions, all of a sudden the number you can get back becomes significant.

Other financial markets are already ahead of us on this one. At the end of every day, every bank will have a zero balance. If it needs money, it will borrow it at the inter-bank rate and if it has too much cash, it will lend it to someone else, again at the inter-bank rate. In other words, it will get rid of every last penny. If you look at the size of monies we are talking about held in reserve in the London market, interest overnight all of a sudden becomes significant.

The comparatively miniscule amount it costs to use a system like the ones available at the moment means they are an obvious solution. You save money because you can allocate resources quicker. You have got the control. And you have not got your broker or underwriter wasting time signing silly forms in a box as it is all done electronically, at the click of a button. Going electronic is the simplest decision you can make.

Despite the baffling talk and difficult-to-understand acronyms used when talking about making the market electronic, the systems available nowadays are remarkably easy to use and simple to operate. It is not rocket science, and it not expensive to implement.

There is a real desire in the market right now to push forward with change, and a feeling that without it we in the market will not survive against more technologically-savvy competition. Customers are demanding better service, and watchdogs and supervisory bodies are looking for clearer audit trails.

Taking on an electronic system that lets brokers, underwriters, customers, lawyers and even third party administrators exchange information is really a no-brainer.

Getting real-time reserves, and managing your money there effectively, could be the golden lining on the dark cloud of the soft market.

Richard Garnett is managing director of Yellowblox.com, an electronic communications system for the insurance and reinsurance industry. www.yellowblox.com