

# BERMUDA

## Insurance Update

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## Captive interest on the rise

Corporate interest in the formation of captive insurers has picked up, particularly as a result of the recent renewal season when insureds were faced with significant increases in insurance premiums, a leading US lawyer involved in the captive industry has said.

Tom Jones, Tax Partner at the Chicago office of global law firm, McDermott, Will and Emery, was speaking with the *Update* after emerging from the International Captives Congress (ICAP 2001).

He said, "A lot of people thought about a captive, but put it on the back-burner. There are CFOs who knew they needed a captive, but they didn't need it next week. They had a lot of other pressing issues to deal with

"But now, with the July 1 insurance renewals, they've seen the rate increases, and all of a sudden the captive concept has moved from the back burner to the front burner.

"So I foresee a spate of new captive formations through to the end of the year. No question, it will be market driven. But you have to get the co-operation of reinsurers. Retrocessionaires in a hardening market will make it a little more difficult."

Mr. Jones also commented that Bermuda's lack of a corporate income tax will become less of an issue in the near future, after lengthy inquiries by various bodies. He said that there will be a consensus that the lack of such a tax structure is not a bad thing.

Offshore jurisdictions have come under intense scrutiny by the Organisation for Economic Co-operation and Development (OECD), the Financial Action Task Force (FATF) and the Financial Stability Forum (FSF). A UK-led study of offshore financial centers was also conducted by the global accounting firm of KPMG.

Mr. Jones said, "There are other ways to collect revenues for a government, whether it be an employment tax or customs duties. And no one country or group of countries have the unfettered authority to tell other sovereign nations what they



Tom Jones

should or shouldn't be doing in regards to their domestic tax situation.

"So I think that the issue will be in the press for the next few months, but will eventually fade away. I think there will be continued discussions about the issue of money-laundering globally, but jurisdictions like Bermuda have nothing to fear in that regard, because it is in compliance with international norms."

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Brian Duperreault

Bermuda reinsurers will do more captive reinsurance for Bermuda captives than in the past, Chairman and CEO of ACE Ltd., Brian Duperreault, told delegates to IBC USA's 5th Annual International Captives Congress (ICAP 2001).

Mr. Duperreault's remarks came during his keynote address to more than 200 delegates at the Fairmont Southampton Princess Hotel in Bermuda in June.

## ACE may woo captives

During a question period after the main address, he characterised Bermuda as an 'insurance powerhouse' which will provide more reinsurance for captive programmes.

He anticipates a growing trend for Bermuda's two, relatively separate, insurance markets to do more business together.

He said, "Most of the publicly traded reinsurers by market value are now located in Bermuda. V.J. Dowling of Dowling & Partners Securities in a presentation made two weeks ago pointed out that

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# Max Re takes stake in new reinsurer

Bermuda-based Max Re Capital Ltd. and Bayerische Hypo- und Vereinsbank AG (HypoVereinsbank) have incorporated Grand Central Re Limited, a Class 4 Bermuda insurance company with an initial shareholders' equity of \$200 million.

HypoVereinsbank has invested \$185 million for 92.5% of the ordinary share capital of Grand Central Re, and Max Re Capital has invested \$15 million for the remaining 7.5%.

Max Re Capital Ltd brings insurance management and underwriting expertise to Grand Central Re, and HypoVereinsbank brings asset management and banking experience.

HypoVereinsbank's Chief Executive Officer for the Americas and Asia, Stephan W. Bub, said "We are excited by the opportunities that Grand Central Re offers



Robert J. Cooney

to HVB Group. It represents a natural extension of our financial services operations, and we are committed to participating actively in Bermuda's innovative reinsurance marketplace."

Robert J. Cooney, Chairman, Chief Executive Officer and President of Max Re Capital said "We view HypoVereinsbank's choice of Max Re to manage the underwriting activities of Grand

Central Re as a strong endorsement of both our expertise and our strategy. We expect the combination of Grand Central Re and Max Re will offer enhanced benefits to our clients."

The adviser and project manager for the Grand Central Re project was ISIS Limited, a corporate finance business based in Bermuda.

Bermuda has one of the largest reinsurance markets in the world, with an indus-

try of some 1,600 insurance and reinsurance companies, with total assets of over \$132 billion and capital and surplus of over \$55 billion.

HypoVereinsbank is the largest real estate financier in Europe and Germany's second largest bank. With a staff of over 72,000 employees and approximately 2,400 branch offices, it serves more than eight million customers and focuses its activities on four core competencies: mortgage banking, asset management, structured finance and selected financial market products. At December 31, 2000, HypoVereinsbank Group assets amounted to 716.5 billion euros.

Max Re Capital is a privately owned Bermuda holding company. Through its operating subsidiary, Max Re Ltd., it offers customized risk financing solutions to life and health insurers, property and casualty insurers, and large corporations. The company's shareholders' equity at March 31, 2001 exceeded \$500 million.

# The Imagine Group acquires Enterprise Re

New Bermuda reinsurance group, Imagine, has moved to snap up reinsurance group, Enterprise Re, a firm with consolidated shareholders equity exceeding \$100 million.

Enterprise Reinsurance Holdings Corporation and all of its subsidiary companies will be integrated into the worldwide insurance operations of The Imagine Group going forward.

Bermudian founder and Co-CEO of The Imagine Group, Thomas Gleeson commented: "The purchase of Enterprise Re furthers the implementation of our very focused business model and is consistent with our previously stated goal of providing a unique financial services platform to the global insurance industry. This transaction further enables The Imagine Group to meet the significant demand for structured insurance and reinsurance products that we are seeing in the marketplace today."

President of Enterprise Re, Jonathan Roberts stated: "The employees of Enterprise Re are very excited about this opportunity. The Imagine Group immediately provides us with greater resources to offer a much broader spectrum of innovative solutions within a dynamic, entrepreneurial and forward-thinking organization."



The Imagine Group founders and Co-CEOs Thomas Gleeson (l) and Brad S. Huntington.

George Gleadall, Chairman of Imagine Insurance Company Limited, the acquiring entity within The Imagine Group added: "This transaction is a building block in the development of our group.

"Following completion of the transaction, the Group will have offices in Barbados, Bermuda, New York, Dublin, Copenhagen, Basel, and St. Louis."

Founder and Co-CEO of The Imagine Group, Brad S. Huntington also commented: "It is indeed rare, in a single transaction, to be able to add such a seasoned and talented group of finite-risk professionals

as is found within Enterprise Re.

"The addition of Jon Roberts and his team brings the employee count of The Imagine Group to 18 professionals and significantly expands our technical analytical skills and our universe of potential and existing clients.

"It also adds to the already significant production and structuring skill-set within The Imagine Group.

"We look forward to the continued expansion of our franchise going forward and extend a warm welcome to all of the employees of Enterprise Re."

The Imagine Group is 100% ultimately owned by Trilon Financial Corporation and Management.

Trilon Financial Corporation is a major Canadian financial services company that provides a broad range of financial and management services to its clients.

Trilon also has extensive ownership experience in the insurance and reinsurance marketplace.

The Imagine Group is a next generation finite-risk reinsurance enterprise whose products deliver structured insurance and reinsurance capital solutions to its clients.

On June 18, 2001, Imagine Insurance Company Limited was assigned an "A" (Strong) rating by Fitch IBCA, Duff & Phelps.



# ASHRM winner arrives

Janis and Dean Matthys vacationed in Bermuda this spring, courtesy of key partners to the Bermuda Insurance Market: Delta Air Lines, the Fairmont Southampton Princess Hotels and PricewaterhouseCoopers (PwC).

Mr. Matthys, RN, MS, the Director of Risk Management Services for Methodist Hospitals of Dallas, won the trip for two as a participant in a promotional draw mounted by the Bermuda Insurance Market during the American Society of Healthcare Risk Management of the American Hospital Association (ASHRM) Conference in New Orleans in November.

At the start of their Bermuda holiday, the couple met Roger Gillett, the Chairman of the Marketing Committee of Bermuda's Insurance Advisory Committee (IAC) and PwC partner, Richard Patching, himself a member of the Marketing Committee.

The promotion was an effort to attract more attention to the Bermuda exhibit during the ASHRM Conference. The strategic partners agreed to offer two free air tickets (Delta) and a three night stay in Bermuda (Fairmont Southampton Princess Hotel)

based on a business card draw from those who visited the Bermuda booth at the show.

PwC agreed to provide cash to help defray the cost of meals. This week's meeting was an opportunity for Mr. Patching to congratulate the couple and present them with the cash.



Roger Gillett (left) and Richard Patching (right) meet Janis and Dean Matthys.

The ASHRM Conference brings together risk managers and other insurance buyers from major hospitals and other healthcare providers. Bermuda is one of the largest providers of captive insurance to the healthcare industry.

Bermuda remains, by far, the dominant

captive insurance domicile in general, having attracted some 1,200 captives, nearly 30 percent of the global total.

Mr. Gillett welcomed the couple to the Island, observing that Bermuda had been attending the ASHRM Conference for several years.

He said, "We believe that risk managers in the healthcare industry are looking more and more to alternative market solutions when it comes to risk financing and have

been extensive users of captives. Many select Bermuda as their domicile.

"The ASHRM Conference is therefore an opportunity for Bermuda firms to show the available expertise that exists in the local market."

Mr. Patching said PwC was delighted to be involved in the Bermuda Market promotion, particularly because of the firm's prominent role in servicing the Bermuda insurance industry.

He said, "We see the Bermuda Market as an important element of the

global insurance community, providing specialised expertise to an increasingly particular corporate risk management professional. The healthcare industry, like many others, recognises the substantial position occupied by Bermuda on the world insurance landscape."

# Harrington changes hands, elects new Board

Harrington International Insurance Ltd. has become the major risk carrier of Strategic Risk Solutions (SRS), the dedicated corporate bancassurance unit within the Winterthur and Credit Suisse Groups.

The move came as a new board was elected following the acquisition by Winterthur Swiss Insurance Company of Swiss Reinsurance Company's 71.4% interest in Harrington Holdings Ltd., and its subsidiary Harrington International Insurance Ltd., at the beginning of the year. Winterthur had assumed management responsibility as early as last September.

SRS originates, structures, and underwrites highly structured financial and operational risk programs for large corporations and selected financial institutions. Harrington will serve as the "cornerstone" of SRS's global operations.

The new board now consists of John Dacey, Chairman J. Brady Young President and CEO, Peter Manz, Ned Bowers, Brent Clark, Vincent Fleury, Mark Romano and

Timothy Faries.

John Dacey serves as CFO of Winterthur Swiss Insurance Company. Peter Manz is Head of Risk Management for Winterthur. Ned Bowers, Brent Clark, Vincent Fleury, Marc Romano and Brady Young are Executive Directors of Strategic Risk Solutions (SRS). Timothy Faries is head of the Insurance Practice group at Bermuda law firm Appleby, Spurling & Kempe.

They replace John O. Austin, former Chairman of the Board of Harrington and retired General Manager of Mercantile and General's world-wide non-life operations, Hans Gmuender, Executive Board Member, Winterthur International, Hans Hefti and Hans-Kaspar Zulauf, principals of Swiss Re New Markets, and Lynda Milligan-Whyte of Bermuda law firm Milligan-Whyte & Smith.

"We are indebted to the support and guidance that these directors provided to Harrington," said J. Brady Young. "They

were all part of Harrington's original board serving from the time of the Company's formation in 1995. They were instrumental in establishing and building the company."

"We are very pleased to have acquired Harrington from Swiss Re," said Mr. Young. "The acquisition is a further step in broadening the global operations and presence of Winterthur and SRS. It will strengthen our abilities to deliver to our clients tailor-made solutions to a variety of complex risk financing problems."

"We very much look forward to being part of the dynamic and growing Bermuda market," said Marc Romano, Senior Vice President and Chief Risk Officer of Harrington. "Harrington will complement the group's strong worldwide franchise and provide a platform for creativity as we seek new ways to deliver comprehensive risk solutions to our clients."

Harrington International Insurance Ltd. is a Class 3 insurer.

# Government pledges market support

The Bermuda Government has signaled an intention to continue legislative and policy support to maintain the Island's international insurance industry as a global leader in the provision of insurance services.

In opening the ICAP 2001 Conference, Premier Jennifer Smith stated: "My Government is committed to working with the international business industry to continue to refine our legislative and regulatory regime.

We understand that it is essential to create the right environment for the conduct of sound, stable reputable business. And we are fully aware that Bermuda cannot afford to become complacent if we want to retain our position as a leading international center for offshore companies.

"It is clear that word of Bermuda's attractiveness as a financial center has spread, for listed among the ninety four new insurance companies added to the register last year, are companies from such non-traditional regions as Brazil, Norway, The Netherlands, South Africa and France.



Premier Jennifer Smith

"Overall, Bermuda's business environment -- and the economic benefits it brings -- continues to grow, so that the total number of insurers now registered locally is fifteen hundred and sixty-four.

"A year ago (during last year's ICAP opening address), I expressed confidence that Bermuda would weather the storms that seemed to be accumulating for international financial service centers.

"I am happy to say that Bermuda's history and ongoing practice of upgrading our regulatory framework continually, coupled with our proactive "Know Your Customer" philosophy, have passed the most stringent tests. The interests of existing clients, future clients, and the interest of Bermuda as a whole, have been, and remain, protected.

"Throughout our history, Bermuda has adapted to the changing needs of the marketplace. And it is clear as we look to the future, that the jurisdiction that adapts and conforms to the highest international

standards will be the most highly regarded and thus stand out as the most favourable base for legitimate business.

"We remain confident that Bermuda will continue to more than meet that challenge."

The Premier also reiterated a theme she began earlier in the year. She said that as a jurisdiction, Bermuda is constantly developing and adapting to the challenges that face business communities globally. It does so by building solid relationships between government and the business community.

This relationship, she said, blending the skills and mindset of public and private sectors, allows us to ensure that the business community operates with a sound regulatory framework of the highest standard, in an environment that fosters innovation, growth and prosperity

Premier Smith added, "Bermuda is widely acknowledged as a center of excellence for Risk Transfer, Investment Acumen and, most recently, E-Commerce. Overall, Bermuda's economy and business environment continues to grow. As of December 31, 2000, there were more than thirteen thousand international companies registered in Bermuda, an increase of nearly ten percent over the total in 1999.

## Regulators face emerging issues

Insurance regulators from Bermuda and other insurance jurisdictions agreed that increasingly sophisticated consumers and business activity have led to the development of newer and more complex insurance products.

The panel of regulators at ICAP 2001 included Bermuda's Registrar of Companies Jeremy Cox; Assistant Director of Captive Insurance, Vermont Department of Banking, Insurance, Securities and Healthcare Administration, Derrick White; Craig Watanabe from Hawaii's regulator's office; and, Clayton Ingram of the regulator's office in South Carolina.

Karen Goldman, Director of Risk Management at Whitman Corp./Pepsi-Cola General Bottlers, Inc., and moderator Malcolm Butterfield, Principal at KPMG, a former Bermuda regulator joined them.

While Ms Golden was also Chairman of the Conference, she helped the panel focus on the question: Is respect for insurance regulations growing or diminishing?

Mr. Cox opened dialogue on the evolution of regulation, through the changes in the industry. He said, "Regulation is changing, just as the market is changing.

"Bermuda recognised this, and in 1995

made significant changes to our legislation, to take us from one set of rules for the entire industry, to a stratified system of classification - providing different levels of regulation for different types of insurance companies.

"We have developed a substantial reinsurance market, which led to the need for evolving regulation. Bermuda has become a one-stop shopping opportunity, with a sound infrastructure and the luxury of close proximity to the US. In addition, there is access to a reinsurance market that has strong intellectual and financial capital behind it."

The panel also agreed that current regulatory legislation allowed regulators to exercise a fair amount of discretion when dealing with insurers. Panellists said that it has led to more questions being asked of the regulator's office.

A key strength highlighted for effective regulation was the Bermuda model, where there has been a long-standing partnership between business and regulators.

Mr. Cox said, "It doesn't mean that we rely on them to do our job. We have a significant role. But it allows us to get infor-

mation we are looking for. Still, we have a higher calling. We are responsible for the country's reputation and policyholder interests."

Craig Watanabe agreed, stating that Hawaii depends a lot on the private sector as well, when it comes to regulating insurance companies.

Mr. Ingram from South Carolina said his jurisdiction was looking at opportunities for de-regulation. He said, "A great deal of our legislation was based on Vermont. But we are now looking at the Bermuda model of regulation for the future. We are going after more alternative market business."

Meanwhile, British Virgin Islands regulator, William McCullough, who observed the session as a member of the audience, concurred with Mr. Cox, that regulators have to be mindful of international standards being set by global bodies, such as the International Association of Insurance Supervisors (IAIS).

They agreed that it was an issue that was becoming increasingly relevant.



Jeremy Cox

# Authorities tackle money laundering

Bermuda regulators have a track record of working with their counterparts in other jurisdictions to stem illegal transactions, an ICAP session on how anti-money laundering initiatives will impact captives was told.



Patrick Hackenberg

And Tax Associate with KPMG Bermuda, Patrick Hackenberg, said that money laundering practices are not exclusively an offshore activity.

He said, "Over the last couple of decades, issues surrounding money laundering have surfaced onshore. It's been demonstrated that New York and other US financial centres had trouble determining the actual source of funds. There are now particular controls being put into place by all the US banks.

"Bermuda has had capable regulation for some time and that's contributed to the lack of money laundering cases here. Bermuda regulators have been noted, in

that they have made other regulators aware of suspicious transactions."

Mr. Hackenberg noted that Bermuda had survived a slew of investigations into offshore financial centres, including the latest KPMG report commissioned by the British Government.

He said, "Bermuda emerged from the KPMG report with flying colours, and has seriously addressed the suggestions for potential improvements. "Captives are meant to manage risks, reduce costs and minimise regulatory burdens. Other jurisdictions, including South Carolina, Hawaii, and Vermont, have realised that the way Bermuda does things sets the international standard."

The panel was entitled "How will anti tax haven/anti money laundering initiatives impact captives?" The panel evaluated the recent initiatives of the Organisation for Economic Co-operation and Development

(OECD) and the Financial Action Task Force, and their potential impact on legitimate offshore based businesses, such as captive insurers.

The panel was moderated by Tom Jones, Partner with McDermott Will & Emery. It included Mr. Hackenberg, Michael Zeldin, a Deloitte and Touche Partner who is the former Chief of Money Laundering and Asset Forfeiture with the US Department of Justice, and, Amy Rudnick, Partner with Gibson, Dunn and Crutcher LLP who is the former Director, Office of Financial Enforcement with the US Department of Treasury.

The panel looked at the future of the offshore financial world, discussed the issue of whether or not G7 nations will impose equally strict standards and penalties on their own financial institutions, and offered suggestions on how captive boards can avoid even the erroneous hint of impropriety.

# Best targets captives for insurance ratings

There is increasing interest in an A.M. Best rating of Bermuda captive insurers by captive owners. Best's Assistant Vice President and Managing Director - Alternative Markets, Carol Pierce said, in 1999 Best put together an ART group specifically to focus on captive and other alternative risk mechanisms.

Ms Pierce was speaking during an ICAP discussion of how and why to obtain a financial strength rating for a captive. Best rated 135 captives by the end of 1999, but added an additional 60 by the end of 2000.

She said, "The other big push was to be able to capture data and format it with the view to giving it back to the captive industry, giving them some meaningful benchmarking data. It is something that is totally missing in the market, and something most other industries would have access to."

The push by Best to rate more captive insurers meant special emphasis on the international or non-US market, which includes Bermuda.

"We had to spend time in some of the offshore jurisdictions, familiarising ourselves with their regulations," she said.

But A.M. Best wants to devise a methodology to look at segregated cell companies, so that they can be approached in the future.

Said Ms Pierce, "There are differences among the jurisdictions, so we won't have a one-size-fits-all approach. In some juris-



Carol Pierce

dictions we're going to take an approach similar to Lloyd's, looking at the entire enterprise.

"We are looking at, and have been asked to rate, individual cells. But in that case, they have to meet our minimum criteria,

which many won't. Maybe we can just apply the enterprise group methodology that we have to those particular companies.

We really need to come up with a published set of criteria on how we look at them, and what are going to be the key components. That's a work in progress now. We hope to have some form of bare bones structure for that by the end of the year. It will probably not be a static thing, in that it will more than likely evolve from there."

At the end of 2000, Best had letter ratings for 66 Bermuda insurers in addition to ratings for 35 Not Rated (NR) companies. NR ratings are assigned predominantly to small companies for which A.M. Best does not have sufficient financial information

required to assign a rating opinion. The information contained in these limited reports is obtained from several sources, which include the individual companies and the National Association of Insurance Commissioners (NAIC).

Best has letter ratings for 29 Bermuda captives out of the roughly 1,200 registered on the Island and 15 in the NR category.

The objective of Best's rating system is to provide an opinion as to an insurer's financial strength and ability to meet ongoing obligations to policyholders. Opinions are derived from an evaluation of a company's balance-sheet strength and operating performance as compared with Best's quantitative and qualitative standards.

Best assigns to insurance companies one of two types of rating opinion, a Best's Rating (A++ to F) or a Financial Performance Rating (9 to 1).

The Best's Rating represents an opinion based on a comprehensive quantitative and qualitative evaluation of a company's financial strength, operating performance and market profile. The FPR represents an opinion based primarily on a quantitative evaluation of a company's financial strength and operating performance for companies that do not meet A.M. Best's minimum requirements in size and/or operating experience.



# ACE, XL move into new homes

Two significant insurance buildings were scheduled for completion this summer on the edge of the City of Hamilton. Two global insurers and reinsurers, ACE Ltd. and XL Capital Ltd, were busy moving staff into brand new offices on the five acre site that was once home to a prominent Bermuda hotel.

These two state-of-the-art insurance buildings were being completed after the Zurich Building, another 100 million-dollar-plus development, was completed on Pitt's Bay Road.

But amazingly, with the significant interest by companies moving to Bermuda, the office space being vacated is getting quickly snapped up. Bermuda's commercial realtors have conceded that the turn-over has been surprisingly quick.

In fact, the 430 people being moved by ACE and XL Capital into the new office blocks were leaving office space that had been spoken for months before. Experts said that the same thing happened recently when the huge Zurich Insurance Building came on line on Pitt's Bay Road.

Ian Waddington, General manager of Coldwell Banker JW Bermuda Realty, said, "The demand for top quality space is still very high in the city. There are a number of companies that see Bermuda as a prime place to move to, so every day we are seeing new operations coming onto the island.



*An artist's impression of Phase 1 of the new ACE Building.*

While these are mainly insurance and insurance-related businesses, there are other types of business that also find Bermuda as a useful business domicile."

One city office building, Cumberland House, had XL and Centre Solutions as

tenants, before the move, taking up seven and a half of the nine floors. But before they left, the buildings owners were already turning people away.



*An artist's impression of the \$115-million XL House.*

Jack Chiappa, who is knowledgeable about the city's premium office space, said, "There is no space available whatsoever at Cumberland House. There is not one square foot available at Craig Appin House, the Chevron building or Dorchester House."

And Mr. Waddington added, "I don't see any sign that there will be any abatement in the longstanding high demand for quality commercial space."

Meanwhile, the first of the two new buildings to be completed was XL House, described as the largest building project carried out in Bermuda in the last 30 years. It is the new global headquarters of XL Capital Ltd and was completed at a cost of approximately \$115 million. The main entrance is on Bermudiana Road.

The cost includes original purchase, demolition, construction of two levels of underground parking facilities for up to 210 cars and 190 bikes, two office buildings totaling 286,000 square feet.

Initial work began almost four years ago to the official opening day on May 10 with the erection of perimeter security fencing in May 1997. Demolition started shortly thereafter.

Some 270 personnel, who make up XL's Bermuda operations, have settled into the generous office space where there is room for growth.

A key XL House feature and attraction to visitors, including local school students, is the fish tank in the lobby that represents typical life on Bermuda's reefs. The capacity of the tank is 10,000 gallons making it one of the largest private fish tanks on display.

While realistic in appearance, all the

corals and sponges are synthetic. This provides a stunning sight while preserving the environment.

Meanwhile, Bermudians have also watched with interest the concomitant building project going on just next door, for the new ACE Global Headquarters (Phase 1). Ground was first broken for the project in August 1998.

The address of the new ACE Global Headquarters is 17 Woodbourne Avenue. The main entrance is located on

Woodbourne Avenue, the first road outside the City's western limits. An official opening was scheduled for August once all employees had moved in. ACE was formed in 1985, with its first employee writing the first policy out of an hotel room.

ACE employees this year, were located in five locations around the city. This July, their move-in schedule included relocating 160 people. There are four floors of office space totalling approximately 75,000 square feet. In addition there are two levels of underground parking space for ACE employees.

The first phase of the development comprises about 180,000 square feet. Architects are the Hillier Group (Washington) and Conyers & Associates (Bermuda). Interior design was by Design Tech.

## Arch buys Altus

Bermuda-based Arch Capital Group Ltd. set aside \$36 million to buy alternative risk transfer provider Altus Holdings Ltd., making it the sole Altus shareholder. Arch Capital provides a whole range of risk transfer and risk financing services for the insurance and reinsurance industry.

Altus was formed in 1998 to provide rent-a-captive and other underwriting management services for risks of individual corporations and insurance programs developed by insurance intermediaries.

Stockholders at the time, in addition to Arch, were the Trident Partnership, L.P., XL Capital Ltd., MMC Capital, Inc. and members of Altus management.

The acquisition is the latest in a series that is completely recreating Arch Capital, under the leadership of President and Chief Executive Officer Peter Appel and Chairman Robert Clements.



# Sovereign helps light up Brazil

Sovereign Risk Insurance Ltd. and the Inter-American Development Bank (IDB) has signed a contract to provide reinsurance for a private sector guarantee issued by IDB for the Light project in Brazil.

Sovereign's \$50 million reinsurance policy supports the IDB's Political Risk Guarantee issued to Citibank, N.A., as trustee for a bank syndicate, under an indenture between Citibank and the issuer, Light-Servicos de Eletricidade S.A., a company incorporated under the laws of the Federative Republic of Brazil.

The indenture governs the issuance of promissory notes, the proceeds of which will be used to finance Light's investment program to improve electric service and coverage in the State of Rio de Janeiro.

The \$100 million IDB guarantee covers risks associated with currency inconvertibility, transferability and funds expropriation. Under the reinsurance policy, Sovereign assumes a portion of the guarantee risk.

Use of reinsurance is one way in which IDB seeks to leverage its resources and enhance its capabilities to guarantee private sector transactions in its member countries. This is the second time IDB has used private sector reinsurance, and it follows the model used for the VBC transaction, also in Brazil, that closed earlier this year. Sovereign was the reinsurer for the VBC contract as well.

Mr. Hiroshi Toyoda, Manager of IDB's Private Sector Department, noted that reinsurance enables the IDB to leverage its own resources to better support private sector operations in the IDB's member countries throughout Latin America and the Caribbean.

"We are delighted to be working with Sovereign as they are one of the world's leading political risk insurers and have the experience and financial strength to complement our private sector operations," he said.

Price Lowenstein, President and Chief Executive Officer of Sovereign, commented that he was "very pleased to close a second reinsurance transaction with the IDB. We believe this transaction, along with the VBC transaction, signals the beginning of an exciting, mutually beneficial relationship between Sovereign and the IDB. We look forward to future transactions supporting the IDB's Guarantee Program."

The Inter-American Development Bank was established in 1959 to help accelerate

economic and social development in Latin America and the Caribbean. With an active loan portfolio of \$49 billion and 46 nations as members, including 26 beneficiary countries in Latin America and the Caribbean, it is the largest and the oldest regional multilateral development institution. In 1995, the IDB was authorized to funnel up to five percent of its ordinary capital resources to the private sector without government guarantees, complementing its lending in direct support of economic and social development.



Price Lowenstein

Sovereign is a specialized political risk insurer and reinsurer based in Bermuda. Sovereign's portfolio exceeds \$4 billion of exposure spread over 60 emerging markets. Sovereign's clients include financial institutions, national export credit agencies, multi-

lateral institutions and multinational corporations. Sovereign is a joint venture between XL Insurance Ltd, a wholly-owned subsidiary of XL Capital Ltd and ACE Bermuda Insurance Ltd., a wholly-owned subsidiary of ACE Limited.

Sovereign recently completed two political risk insurance policies for capital markets transactions. One policy was issued in support of a \$95 million securitization of Senior Mortgage Bonds on behalf of BACS I Mortgage Trust. The bonds are backed by US Dollar-denominated mortgage loans secured by residential properties in Argentina.

The issuer, Banco de Credito y Securitizacion S.A. (BACS) is an Argentine financial entity formed in September 2000 by the International Finance Corporation, Banco Hipotecario SA and Inversiones y Representaciones SA to create and develop the secondary mortgage market in Argentina. The senior bonds were part of the \$115.8 million BACS I 2001-1 issue of mortgage bonds, which is BACS' first issue since its formation.

The 12-year political risk insurance policy covers up to 15 months of interest payments on the notes against the risks of currency inconvertibility and currency nontransfer.

Moody's assigned an "A1" rating to the senior bonds, which is the highest rating

that can be assigned to a cross border bond supported by Argentine assets, while Fitch Inc. rated the transaction "A+". These ratings are 9 notches above Argentina's sovereign ceiling for Moody's and 7 notches for Fitch Inc.

Mr. Lowenstein stated: "We are pleased to have been able to assist BACS in achieving an investment grade rating on this transaction. This marks both a continued expansion of Sovereign's product development and a further evolution in the use of political risk insurance in the capital markets. We are confident that political risk insurance will be increasingly utilized to meet the need to elevate the ratings for emerging market securitizations above the sovereign ceiling in sub-investment grade countries."

Sovereign completed its first political risk insurance policy for a capital markets transaction in February. The policy was issued in connection with a \$234 million offering of notes due 2015 issued by the Salta Hydrocarbon Royalty Trust.

## A-Rating for mutual

A.M. Best Co. has affirmed the A (Excellent) financial strength rating of Steamship Mutual Underwriting Association (Bermuda) Ltd. The rating action reflects the maintenance of the club's leading position within the International Group and the protection and indemnity industry, strong capital position and extensive reinsurance protection.

Offsetting factors include the continuing competitive pressures in global insurance and reinsurance markets and the deterioration in the club's operating performance for the year under review.

Steamship Mutual had retained and built upon its leading successful position in the P&I market. Entered tonnage remained relatively unchanged at 64.1 million, compared with 64.5 million in 1999, and ranked Steamship fourth in the International Group of Clubs.

Diversification on a geographic, vessel-type and business-class basis was maintained, and management continued to be proactive in establishing new business ventures and launching innovative products.

In addition to the creation of Portsure in 1999--a joint venture with Brockbank to provide coverage for ports--the next year the club's management established Origin Ltd. with Associated Electric & Gas Insurance Services (AEGIS).



# Captives on the rise

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Mr. Jones said that people looking to form captive insurers rarely are concerned about these issues.

He said, "Governmental organisations and public entities, such as state universities, may look at going offshore as a political thing. But otherwise the onshore/offshore decision is not in any way affected by perceptual issues....and even less in Bermuda because with just three banks, the island is not a major offshore banking center. The public image of alleged nefarious activities tends to center on places that have multitudes of banks."

Mr. Jones said that the investigation of offshore centers may have been designed to allow the larger nations to educate others, but ended up with the larger nations themselves learning much about the offshore world.

He added, "It made them understand that they needed to distinguish specific offshore jurisdictions from others. There are some offshore financial centers that treat the particular issues, such as tax harmonisation and money-laundering, a lot differently from others. My guess is that the teachers have learned as much as the students."

Thomas M. Jones is a partner in the Tax Department in McDermott, Will & Emery's Chicago office. His practice focuses on US federal tax and corporate planning, largely in an international context, and in tax, regulatory and other legal matters concerning self-insurance and other alternatives to commercial insurance. He works with U.S.-based multinational corporations, foreign investors, health care providers, joint ventures and domestic businesses of all sizes.

# ACE to reinsure captives

■ continued from page 1

Bermuda companies accounted for 81% of \$21 billion in outstanding market value of the remaining independent publicly traded reinsurance companies. Ten years ago, Bermuda companies accounted for only 20% of the market value of publicly traded reinsurers.

"Quite a change... and I can assure you it wasn't because of taxes."

The Bermuda Market was originally no more than the leading domicile for captive operations before the nineties when it began to develop a strong presence in the global reinsurance arena. Mr Duperreault noted that so far there has been remarkably little interaction between the two Bermuda markets.

He said, "I find it fascinating that Bermuda houses the largest captive market in the world and the most innovative reinsurance market, and yet the two do almost no business together. Both grew independent of each other but will market forces change this? I think they should."

"As rates rise, captives will take on more risk, that is one of their primary functions. But how do you deal with volatility? Does the parent really want this risk? It certainly doesn't want its short term effects. Reinsurance rates are rising at least as fast as the primary so there is no relief there. I mentioned that this is a globally hard market so there is no safe haven of capacity."

"Where does the captive go? Who are the world leaders in ART? - to the Bermuda insurance companies who specialize in the solutions business. Maybe it isn't ironic."

"Maybe it is the natural course of events, but I believe that we'll see these two world class markets who live side by side on this very small Island finally do business together."

Despite the soft market of recent years which usually signals a reduction in captive activity, the Bermuda captive market continued to grow. And rates are now on the rise.

He believes that the hardening market could be hard for some time, after captive growth occurred during the long, soft market.

"Captive insurance," he said, "is a very effective risk management mechanism. And we see more captive business coming to us. It makes sense that captives would seek out Bermuda reinsurers, which have a strong reputation for innovation and creativity."

"Bermuda is the place you want to be, if you are in the insurance business. The most professional insurance companies are in Bermuda. I'm talking about companies that actually manage their capital and make an underwriting profit."

In discussing the convergence of the insurance and capital markets, the chief executive remarked that insurance instruments had proven to be more flexible than capital market instruments.

Asked about ACE's significant diversification along business lines, he said, "We will extend into more areas. We've recently gone into Egypt and will develop more business in the Middle East."

The captive conference included workshops on the fundamentals of captives, investment strategies, employee benefits, regulation and recent tax developments. The three-day event also included sessions on cell companies and rent-a-captives, association captives, derivatives and captive reinsurance.

## Hannover Re in new Bermuda reinsurer

Hannover Re Group has established a property catastrophe reinsurance subsidiary in Bermuda. The Hannover, Germany-based reinsurance group's new unit, Hannover Re (Bermuda) Ltd., will write property catastrophe excess-of-loss business and plans to develop a proprietary catastrophe simulation model.

Hannover Re (Bermuda), which has shareholders equity of \$223.3 million, joins a string of other property cat reinsurers in Bermuda. Konrad Rentrup will be managing director of the new Hannover Re unit.

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