

BERMUDA
– A MODEL FOR SUCCESSFUL INSURANCE REGULATION –

*AN UPDATE ON THE BERMUDA INSURANCE REGULATORY ENVIRONMENT
AND THE INSURANCE AMENDMENT ACT 2004*

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Once thought of as solely a jurisdiction for captives, reinsurance and the alternative risk market, Bermuda has developed into the world's most successful and competitive insurance marketplace with significant insurance and reinsurance markets. It is targeted as a growth area by very large players who operate in all major insurance markets and write all classes of business. Bermuda has become a frontrunner in developing innovative ideas to address many of the insurance problems which face business today.

Bermuda calls itself "*the risk capital of the world*," boasting nearly 1,300 insurers and reinsurers with \$63 billion in gross premiums and capital and surplus of more than \$75 billion.ⁱ The stocks of insurance companies in Bermuda have fared much better than in the United States. A review of the financial results of the Bermuda Insurance Index (BII) will reflect better performance than the S&P Insurance Index (S&PII). A five-year comparison of results shows a 94.13% return for the BII contrasted with a 29.33% return for the S&PII.ⁱⁱ

Insurers are attracted to Bermuda because it generates shareholder value. Those insurers operating in Bermuda are attracted to the favorable tax and regulatory environment where there is less frictional capital costs. Additionally, the options are endless for the creation of new capital and new products. Regulation of insurance is moving toward a risk-based regulatory approach rather than a solvency-based regulatory approach utilized in most jurisdictions. This means that the Bermuda Monetary Authority ("BMA") assesses an insurer's risks and identifies areas of its operations which need to be modified to minimize events which would result in an adverse impact on policyholders and the marketplace as a whole.

The Insurance Act 1978, as amended under the Insurance Amendment Act 2002 and the Insurance Amendment Act 2004, provided the Insurance Department with additional powers to obtain information and reports, and to require the production of documents from licensed insurers, insurance managers and intermediaries. The entire Act essentially strengthens previous law by providing the BMA with more power to independently regulate all sectors of the insurance industry operating in Bermuda. In Bermuda, there is solid insurance regulation coupled with a close relationship with insurance industry professionals who advise regulators. The insurance regulatory environment is unique in that it has an Insurance Advisory Committee ("IAC") which is a statutory body that advises the BMA. Insurance is regulated by the BMA. The BMA is responsible for the licensing, supervision and regulation of financial institutions in Bermuda, including insurance. Specifically, the Insurance Department of the BMA is responsible for the supervision, regulation and inspection of Bermuda's insurance companies and for the licensing of all insurance brokers, agents, managers and salesmen.

INSURANCE ACT 2004

The passage of the Insurance Amendment Act 2004 reflects the interest of Bermuda's regulators to continue to be viewed as a strong insurance regulatory environment that works cooperatively with industry. The Insurance Amendment Act 2004 amends the 1978 Insurance Act beyond the 1995, 1998, 2001 and 2002 amendments, by increasing regulatory oversight. The Act codifies the current practices of the Bermuda insurance marketplace and is not likely to increase the regulatory burden on companies but rather eliminate any questions they may have regarding current law and practice. Specifically, the Act relates to four primary areas: (1) timeframes for reporting; (2) hiring and approval of outside specialists; (3) the requirements and obligations of outside specialists; and (4) clarification of regulations on delivery of statutory financial returns.

The underlying basis for the Insurance Amendment Act 2004 was a nine-month review of Bermuda's financial services regulation by the International Monetary Fund ("IMF"). There were suggestions that the insurance regulatory structure was inconsistent with the other financial services statutes.ⁱⁱⁱ The recommendations can be found in the two volume report issued in March of 2005. It, among other things, assessed the Bermuda insurance industry and made suggestions for change which are reflected in the new Act.

The legislation was passed by both the House of Assembly and the Senate of Bermuda in November 2004. The Governor of Bermuda assented to the Act on December 10, 2004. The passage of the Act followed months of meetings between the BMA and representatives of Bermuda's insurance industry to hammer out language which strikes a balance between ensuring strong financial standards, competitiveness and efficiency.

REVISIONS TO REPORTING TIMEFRAMES

Notification of Change in Particulars

The Amendment Act reduces the time that an insurer must notify the BMA of any change in particulars of its principal representative, insurance manager or approved auditor, or any change in the location of its principal office from 21 days to 14 days.

Notification by Principal Representative

The Amendment Act places an obligation on the principal representative to verbally notify the BMA immediately if there is a likelihood of the insurer for which he acts of becoming insolvent, and reduces the time for the principal representative to deliver a written report to the BMA from 30 days to 14 days.

Approval of Loss Reserve Specialist

The Amendment Act adds a provision to require the approval of an insurer's loss reserve specialist by BMA. All classes of insurers (Class 1, only when applicable) must submit the loss reserve specialist's background to the BMA for approval. The BMA may also revoke the approval at any time with prior notification to the insurer and the loss reserve specialist.

Approval and Appointment of Auditors

The Amendment Act adds a provision to require approval and appointment of an auditor by the BMA on the basis of criteria that they are fit and proper. These criteria are to be defined in the guidance notes.

Standard for Auditor Independence

The Amendment Act adds a provision to require that no auditor of an insurer may have an "interest" in that insurer other than as an insured. This provision makes the law consistent with the standards in Bermuda's other financial services statutes.

Requirements for Auditor Notification

The Amendment Act requires auditors to notify the Authority in the event of his resignation or removal or material modification to a report on an insurer's statutory financial statements.

Statutory Financial Statements

The Amendment Act requires all insurers to file statutory financial statements on an annual basis. Additionally, all insurers must file statutory financial returns simultaneously. This new language makes clear that the statutory financial statements must be audited annually by the insurer's approved auditor.

Miscellaneous Provisions

The Amendment Act provides that the BMA may vary or delete any conditions imposed upon an insurer at the time of its registration.

The Amendment Act clarifies that husbands of directors fall within the prohibition on loans to directors.

The Amendment Act establishes a whistleblower provision which extends to captive managers and other service providers.

PUBLISHING OF GUIDANCE NOTES BY BERMUDA MONETARY AUTHORITY

The Insurance Amendment Act 2004 also set forth a framework for the creation of guidance notes. The Act is amended to give discretion to the BMA to create guidance on provisions of the act. The guidance notes are intended to clearly identify the requirements for those who must comply with the Act. The guidance notes also address procedures that must be followed. The guidance notes assist in clarifying the scope and implementation of the Act. This is important to those insurers and reinsurers operating in Bermuda in order to fully understand the insurance regulatory system and its new requirements. The guidance notes are not intended to be exhaustive but to set out the BMA's understanding of the law at the time the guidance notes are published. The BMA admits that interpretation of the law is a matter for the courts and there are likely to be other guidelines issued on particular subjects. The guidelines merely reflect the minimum standard that the Authority expects insurers and other relevant parties to observe at all times.^{iv}

The BMA and the Insurance Advisory Committee worked long hours to create guidance notes, and in March 2005 the BMA issued fifteen guidance notes. Early compliance with these guidance notes is fully encouraged but compliance is not mandatory until December 31, 2005.

SUMMARY

The Bermuda insurance community has been cautious in their passage of the Insurance Amendment Act 2004. The legislators, regulators and insurance advisory committee worked diligently to further strengthen regulatory oversight on insurers and insurance-related activities where there is risk to policyholders, yet they encouraged continued development of a viable insurance market. They have successfully created an insurance regulatory system that recognizes that some regulatory oversight is necessary even in a free market economy but have been careful not to be so restrictive that it will result in less competition and stifle innovation. The guidance notes clearly reflect that the BMA is not turning a blind eye to the areas which require stronger regulatory oversight but rather promoting international best practices for the supervision of insurance. It is predicted that the Insurance Amendment Act 2004 will further enhance the balance between strong regulation without additional burden.

ⁱ Gold, J., *Bermuda Insurers Contemplate Consolidation and A Soft Market*, INSURANCE INSIDER, December 15, 2004.

ⁱⁱ Moody, M., *The World's Risk Capital - Bermuda Provides a Strong Regulatory Environment That Allows for Innovation*, ROUGHNOTES MAGAZINE, July 5, 2005.

ⁱⁱⁱ Dyer, B., *The Insurance Amendment Act 2004 – Business as Usual*, CONYERS DILL & PEARMAN, January 2005.

^{iv} www.bma.bm.